

1987

The Close Corporation under Ohio Law

Forrest B. Weinberg
Cleveland-Marshall College of Law

Follow this and additional works at: <https://engagedscholarship.csuohio.edu/clevstlrev>

 Part of the [Business Organizations Law Commons](#), and the [State and Local Government Law Commons](#)

How does access to this work benefit you? Let us know!

Recommended Citation

Forrest B. Weinberg, *The Close Corporation under Ohio Law*, 35 Clev. St. L. Rev. 165 (1987)
available at <https://engagedscholarship.csuohio.edu/clevstlrev/vol35/iss1/9>

This Article is brought to you for free and open access by the Law Journals at EngagedScholarship@CSU. It has been accepted for inclusion in Cleveland State Law Review by an authorized editor of EngagedScholarship@CSU. For more information, please contact library.es@csuohio.edu.

THE CLOSE CORPORATION UNDER OHIO LAW*

FORREST B. WEINBERG**

I.	INTRODUCTION	166
II.	OVERVIEW OF CLOSE CORPORATION LEGISLATION	167
III.	OTHER OGCL PROVISIONS AFFECTING CLOSE CORPORATIONS	173
IV.	"LEGISLATIVE HISTORY" OF 591	176
V.	OBJECTIVE, PHILOSOPHY, AND APPROACH OF 591	178
VI.	EXPLANATION OF 591	181
	A. <i>Eligibility, Formalities, and Termination</i>	182
	B. <i>What Can Be Accomplished by a Close Corporation Agreement</i>	184
	C. <i>Express Limitations on the Scope of a Close Corporation Agreement</i>	188
	D. <i>Other Shareholder Agreements</i>	190
	E. <i>Savings Clause</i>	190
	F. <i>Negation of Traditional Obstacles</i>	191
	G. <i>Enforcement of Close Corporation Agreement</i>	192
VII.	THE NEED FOR ADDITIONAL LEGISLATION	192
	A. <i>Improving 591</i>	193
	B. <i>Share Transfer Restrictions</i>	194
	C. <i>Relief from Shareholder Oppression</i>	196
VIII.	CONCLUSION	206
VIV.	APPENDICES	
	A. <i>Appendix A</i>	208
	B. <i>Appendix B</i>	212
	C. <i>Appendix C</i>	214

The enactment of Ohio's close corporation law in 1981 accomplished one of the most sweeping changes in the history of this state's corporation laws.¹ It introduced a new set of optional rules specially

* Copyright, Forrest B. Weinberg, 1986.

**Assistant Professor of Law, Cleveland-Marshall College of Law, Cleveland State University; LL.B. 1950, University of Cincinnati; LL.M. 1951, Harvard University. Professor Weinberg is Chairman of the Close Corporation Subcommittee of the Corporation Law Committee of the Ohio State Bar Association, and he was the principal draftsman of O.R.C. § 1701.591, the Ohio close corporation statute discussed in this Article.

The author gratefully acknowledges the valuable research assistance of Mary L. Nummela, Esq., member of the Ohio bar (visiting student, Cleveland-Marshall College of Law, Spring and Fall, 1985).

¹ The last major overhaul of Ohio's for profit corporation law was the adoption in 1955 of the original version of the present Ohio General Corporation Law. See Emerson, *The New Ohio General Corporation Law: Some Comments and Some Comparisons*, 24 U. CIN. L. REV.

designed for the close corporation and its shareholders, thus satisfying a pressing need that has been widely recognized for decades. The result is that for most Ohio corporations, the opportunity now exists for the arrangement of internal affairs in a simple and straightforward manner as in the case of a partnership.²

If this is so, it would hardly seem necessary to beat the drums to encourage Ohio's lawyers to use the new law. Yet the reverse is true. The close corporation law does not have automatic application³ and does not replace any part of the preexisting law. To take advantage of it, affirmative steps must be taken beyond those to which lawyers organizing corporations are accustomed. For these reasons and because force of habit and resistance to change have to be overcome, a broad awareness of the opportunities now available under the close corporation law must be created.

The new law will have the major impact it deserves only as the result of initiative taken by Ohio attorneys engaged in the formation and ongoing representation of close corporations. It is hoped that this article will help motivate Ohio lawyers to provide that indispensable initiative.

I. INTRODUCTION

Section 1701.591 of the Ohio Revised Code⁴ is Ohio's close corporation law. It provides, through the use of a "close corporation agreement,"⁵ the

463 (1955). In light of the radical departure from traditional corporation law brought about by the close corporation law, it might well be said that it not only overshadows the 1955 changes, but even those resulting from the adoption of the 1955 Act's predecessor in 1927 and, perhaps, all changes since 1903, when limited liability first became an incident of incorporation. See Davies, *Reflections of the Amateur Draftsmen of the Ohio General Corporation Act*, 12 WIS. L. REV. 487 (1936-1937). (It is interesting that the author stressed the great flexibility of the 1927 General Corporation Act in regard to the close corporation. *Id.* at 488-89).

² For the single shareholder corporation, the new law provides the opportunity for the procedural simplification of internal affairs to make them comparable to those of a sole proprietorship. See Appendix B for a form of single shareholder close corporation agreement.

³ In more technical terms, the law is "enabling," not "self-executing," legislation. See *infra* note 45.

⁴ OHIO REV. CODE ANN. § 1701.591 (Anderson 1985), hereinafter referred to as "591." All further references to various sections of the Ohio Revised Code will be to "O.R.C." followed by the appropriate section number.

⁵ "Close corporation agreement" is defined in O.R.C. § 1701.01(X) by a cross-reference to the three requirements set forth in 591(A). The close corporation legislation of other states refers to a contract of this type by the generic term "shareholders agreement." See, e.g., CALIF. CORP. CODE §§ 186, 300(b) (West Supp. 1980); TEX. BUS. CORP. ACT. ANN. art. 1201-12.32 (Vernon 1980 & Supp. 1984). Ohio's terminology is superior, because it introduces a new statutory term of art which cannot be confused with the broader category of agreements dealing with voting or other arrangements among shareholders, which are governed by common law. See *infra* text under headings "Explanation of 591 - Other

mechanism, first, for implementing unprecedented informality in the functioning of a close corporation and, second, for establishing a legal relationship among the shareholders that is essentially the same as that provided by law for members of a partnership.

The emphasis of this paper will be its treatment of 591. However, a broader focus will be the legal status of the Ohio close corporation, in terms of where it has been, where it is now, and where it should be going.

Dealing more specifically with what follows, the article will treat 591 in depth, including its text and background.⁶ To provide perspective, the development of close corporation legislation generally and in other jurisdictions will be briefly discussed.⁷ To fill out the contours of the Ohio law, the article will summarize other provisions of the Ohio General Corporation Law (referred to below as "OGCL") having a special effect on the close corporation.⁸ Finally, the writer will consider and recommend improvements to Ohio's laws pertaining to close corporations,⁹ consisting principally of legislation to provide self-executing relief from shareholder oppression.

II. OVERVIEW OF CLOSE CORPORATION LEGISLATION¹⁰

Close corporations comprise the vast majority of all incorporated businesses in this country¹¹ and, thus, the legal issues concerning them are among the most numerous and important confronting lawyers engaged in the business-corporate or general practice.

Although there are a number of published definitions of the close corporation,¹² all the definitions stress certain general characteristics,

Shareholder Agreements" and "Explanation of 591 - Savings Clause." See also *infra* notes 133 and 156.

⁶ See *infra* text under headings "Legislative History" of 591," "Objective, Philosophy, and Approach of 591," and "Explanation of 591."

⁷ See *infra* text under heading "Overview of Close Corporation Legislation."

⁸ See *infra* text under heading "Other OGCL Provisions Affecting Close Corporations."

⁹ See *infra* text under heading "The Need for Additional Legislation."

¹⁰ The special status of the close corporation and its legislative treatment have been the subject of a great amount of legal literature. The preeminent treatise in the field is Professor O'Neal's two-volume work, first published in 1958. F. O'NEAL, *CLOSE CORPORATIONS* (2d ed. 1971). An article by Professor O'Neal appears elsewhere in this symposium issue of the Law Review. Many other articles on the subject are cited throughout these notes.

¹¹ H. HENN & J. ALEXANDER, *LAW OF CORPORATIONS* § 257, at 695 (3d ed. 1983).

¹² "Closely held corporation" is a term used interchangeably with "close corporation." The former may technically be the sounder generic term to cover both corporations that have statutory close corporation status and those that have not. H. HENN & S. ALEXANDER, *supra* note 11, at 695 n.3. The term "close corporation," however, will be used uniformly throughout this article to refer to all corporations falling within the definition, irrespective of special statutory status. Corporations whose shares of stock are traded in the

namely, a small number of shareholders and the absence of any established market for their shares; the active participation by all or most of the shareholders in the business, usually serving as the directors, officers and managerial employees; and the intangible, yet critical, factor of having a closer functional relationship to the partnership form than to the corporate form.¹³

The necessity for special rules of law to accommodate the distinctive needs of the close corporation is well established.¹⁴ In the absence of special laws, the shareholders of a close corporation, who think of themselves as partners, nevertheless find themselves forced into the mold provided by the traditional general corporation law, which also governs the corporate giants listed on major stock exchanges.¹⁵ The basic premise of these general laws is the existence of the corporation as a legal entity separate and distinct from its shareholders,¹⁶ a philosophy that is inherently incompatible with the co-ownership premise of the partnership entity.¹⁷ Thus, it is not surprising that fundamental rules governing the conduct of corporate affairs, which may be beneficial in their application to publicly traded corporations,¹⁸ can cause severe problems and unfair results when applied to the close corporation. Chief among such rules are the principle of majority control¹⁹ and the business

securities market will be referred to throughout this article as "publicly traded corporations."

¹³ See *Estate of Schroer v. Stamco Supply, Inc.*, 19 Ohio App. 3d 34, 482 N.E.2d 975 (1984); *Donahue v. Rodd Electrotape Co.*, 367 Mass. 578, 328 N.E.2d 505 (1975); *Kruger v. Gerth*, 16 N.Y.2d 802, 210 N.E.2d 355 (1965); F. O'NEAL, *supra* note 10, at § 1.02; L. SOLOMON, *CORPORATIONS, LAW AND POLICIES*, at 305 (1982).

¹⁴ See, e.g., F. O'NEAL, *supra* note 10, § 1.13a at 51; Ginsberg, *The Need for Special Close Corporation Legislation in Illinois*, 25 DE PAUL L. REV. 1, 4 n.21 (1975); Note, *The Failure of the Ohio General Corporation Law to Adequately Provide for Close Corporations - Proposals for Change*, 37 U. CIN. L. REV. 620 (1968). Over twenty years ago Professor Bradley stated that the inappropriateness of the general corporation laws for close corporations "has been observed ad nauseum." Bradley, *Toward a More Perfect Close Corporation The Need for More and Improved Legislation*, 54 GEO. L.J. 1145 (1966).

¹⁵ See H. HENN & J. ALEXANDER, *supra* note 11, at 698; SOLOMON, *supra* note 13, at 302.

¹⁶ See H. HENN & J. ALEXANDER, *supra* note 11, § 78, at 146; W. FLETCHER, *CYCLOPEDIA OF THE LAW OF PRIVATE CORPORATIONS* §§ 14, 25 (rev. perm. ed. 1983) (corporate entity is presumed to be separate and distinct whether the corporation has many shareholders or only one); Dickinson, *Partners in a Corporate Cloak: The Emergence and Legitimacy of the Incorporated Partnership*, 33 AM. U.L. REV. 559, 563 (1984).

¹⁷ See UNIFORM PARTNERSHIP ACT § 6 (1910); J. CRANE & A. BROMBERG, *LAW OF PARTNERSHIP* § 14, at 65 (1968).

¹⁸ See Mann, *A Critical Analysis of the Statutory Close Corporation Supplement to the Model Business Corporation Act*, 22 AM. BUS. L.J. 289, 309 (1984); Coffey, Book Review, 23 CASE W. RES. 976, 984 (1972) (reviewing F. O'NEAL, *CLOSE CORPORATION, LAW AND PRACTICE* (2d ed. 1971)).

¹⁹ "[T]he holders of a majority of the shares with voting power control the corporation." F. O'NEAL & R. THOMPSON, *O'NEAL'S OPPRESSION OF MINORITY SHAREHOLDERS* § 1.02 (2d ed. 1985).

judgment rule.²⁰ The effect of these companion principles, when applied to the close corporation, is to deprive minority shareholders of a voice in

²⁰ If in the course of management, directors arrive at a decision, within the corporation's powers (*intra vires*) and their authority, for which there is a reasonable basis, and they act in good faith, as the result of their independent discretion and judgment, and uninfluenced by any consideration other than what they honestly believed to be the best interests of the corporation, a court will not interfere with internal management and substitute its judgment for that of the directors to enjoin or set aside the transaction or to surcharge the directors for any resulting loss.

H. HENN & J. ALEXANDER, *supra* note 11, § 242, at 661.

The general effect of the rule is to discourage interference by courts with decisions made by the corporation's directors and officers. See Peeples, *The Use and Misuse of the Business Judgment Rule in the Close Corporation*, 60 NOTRE DAME L. REV. 456, 459 (1985).

Ohio's codified version of the rule as amended, effective November 22, 1986, appears in O.R.C. § 1701.59, as follows:

(B) A director shall perform his duties as a director . . . in good faith, in a manner he reasonably believes to be in or not opposed to the best interests of the corporation, and with the care that an ordinarily prudent person in a like position would use under similar circumstances

(C) For purposes of division (B) of this section:

(1) A Director shall not be found to have violated his duties under division (B) of this section unless it is proved by clear and convincing evidence that the director has not acted in good faith, in a manner he reasonably believes to be in or not opposed to the best interests of the corporation, or with the care that an ordinarily prudent person in a like position would use under similar circumstances in any action brought against a director, including actions involving or affecting any of the following:

(a) a change or potential change in control of the corporation;

(b) a termination or potential termination of his service to the corporation as a director;

(c) his service in any other position or relationship with the corporation

(D) A director shall be liable in damages for any action he takes or fails to take as a director only if it is proved by clear and convincing evidence in a court of competent jurisdiction that his action or failure to act involved an act or omission undertaken with deliberate intent to cause injury to the corporation or undertaken with reckless disregard for the best interests of the corporation

The purpose of the 1986 amendments was to provide greatly increased protection for directors who resist unfriendly takeovers. While the amendments were being deliberated, concern was voiced by some that these changes might unintentionally facilitate oppression of minority shareholders of a close corporation by the majority in violation of the latter's fiduciary duty. See *infra*, text under heading *The Need for Additional Legislation - Relief from Shareholder Oppression*. To allay the fears expressed on behalf of minority shareholders, there was added to O.R.C. § 1701.59 the following: "(F) Nothing contained in division (C) or (D) of this section affects the duties of either of the following: (1) A director who acts in any capacity other than his capacity as a director"

In *Gries Sports Enter. v. Cleveland Football Co.*, 25 Ohio St. 2d 15, 496 N.E.2d 959 (1986), the Ohio Supreme Court, although sharply divided (four to three) as to the result, nevertheless, in a total of five separate opinions, unanimously assumed that, under Delaware law, the business judgment rule applied to a close corporation. The justices differed, however, as to whether a majority of the directors were disinterested and independent so as to be eligible to claim the benefit of the rule.

the corporation's affairs and to facilitate oppressive action against them on the part of the controlling shareholders.²¹

Early attempts by close corporation shareholders to escape the ill-fitting cloak of the general corporation law were rebuffed by courts. Their thesis was that, having chosen the corporate form, the shareholders were bound by its attributes and could not by agreement vary the corporate norms and thereby conduct their internal affairs as if they were partners.²² Thus, for example, in an oft-cited case,²³ an agreement among shareholders designating one of their number as an officer of the corporation at a stipulated salary was struck down as being an impermissible impingement on the statutory corporate norm conferring exclusive authority on the directors to take such action.²⁴

Following World War II and accelerating since 1960, state legislatures have passed laws to accommodate the special needs of close corporations.²⁵ At the present time such legislation, in one form or another, has been adopted in twenty-one states,²⁶ including most of the leading commercial and industrial states.

²¹ F. O'NEAL & R. THOMPSON, *supra* note 19, at § 1.02, § 3.03.

²² The classic citation for this proposition is *Jackson v. Hooper*, 76 N.J. Eq. 592, 75 A. 568 (N.J. 1909).

²³ *McQuade v. Stoneham*, 263 N.Y. 323, 189 N.E. 234 (1934), in which the agreement in question was among less than all the shareholders. A similar result in a case where all the shareholders were party to the agreement was reached in *Long Park, Inc. v. Trenton-New Brunswick Theatres Co.*, 297 N.Y. 174, 77 N.E.2d 633 (1948).

²⁴ To dispel the notion that the rules established by these older cases lack vitality today when applied to corporations not enjoying statutory close corporation status, see the dissent in *Zion v. Kurtz*, 50 N.Y.2d 92, 99, 405 N.E.2d 681, 688 (1980). It is there stated that "the common law rule applicable to both closely and publicly held corporations continues to treat agreements to deprive the board of directors of substantial authority as contrary to public policy," and that deviations from the corporate norm pose a danger to the public as potential purchasers of the stock. The majority opinion, in upholding the agreement, relied on sections 350 and 354 of the close corporation subchapter of the General Corporation Law of Delaware, which validate an agreement among the shareholders of a statutory close corporation otherwise invalid as an impermissible departure from the corporation norms. For a contrary view, see Easterbrook and Fischel, *Close Corporation and Agency Costs*, 38 STAN. L. REV. 271, 281 (1986) ("McQuade is a fossil. Today courts enforce voluntary agreements of all sorts among investors in close corporations.").

²⁵ O'Neal, *Close Corporations: Existing Legislation and Recommended Reform*, 33 BUS. LAW. 873 (1978).

²⁶ Alabama, ALA. CODE §§ 10-2A-300 to 10-2A-313 (1975); Arizona, ARIZ. REV. STAT. ANN. §§ 10-201 to 10-218 (1977); California, CAL. CORP. CODE §§ 158, 186, 202, 204, 300, 418, 421, 706, 1111, 1201, 1800, 1904 (West Supp. 1980); Delaware, DEL. CODE ANN. tit. 8 §§ 341-356 (1983); Florida, FLA. STAT. § 607.107(2)(1962); Georgia, GA. CODE ANN. § 14-2-120(b)(1982); Illinois, ILL. ANN. STAT. ch. 32, 1201-1216 (Smith-Hurd Supp. 1985); Kansas, KAN. STAT. ANN. §§ 17-7201 to 7216 (1981); Maine, ME. REV. STAT. ANN. tit. 13-A §§ 102.5, 604, 606, 607, 618, 701.2 (1973); Maryland, MD. CORPS. & ASS'NS CODE ANN. § 4-101 to 603; Michigan, MICH. COMP. LAWS ANN. §§ 450.1103(c), 450.1463 (West 1973 J. Supp. 1980); Minnesota, MINN. STAT. ANN. §§ 302A.201, Subd. 2, 302A.457 (West 1985); New Jersey, N.J. REV. STAT.

In 1982, after five years of consideration, the Committee on Corporate Laws of the American Bar Association's Section of Corporation, Banking and Business Law adopted the model "Statutory Close Corporation Supplement to the Model Business Corporation Act (hereinafter "MODEL ACT SUPPLEMENT").²⁷ Recognition of the need for special close corporation legislation perhaps reached its zenith by the action of this prestigious group, which modified its earlier stated position that the requirements of close corporations could be adequately met within the provision of the Model Business Corporation Act generally applicable to all corporations.²⁸

A survey of existing close corporation legislation, including the Model Act Supplement, yields the following inclusive list of the basic objectives of such laws: (1) sanctioning informality in the corporation's internal operations, such as elimination of the board of directors;²⁹ (2) validating an agreement among shareholders covering management and control of the corporation, including protection of the rights of individual shareholders in such areas as employment and sharing profits;³⁰ (3) validating or mandating restrictions on the transfer of shares of the corporation's stock;³¹ and (4) providing remedies for internal strife,³² such as dissension and deadlock and shareholder oppression.³³

§§ 14A.1-1(3)(C), 14A.5-21(2)(6)(West & 1969 Supp. 1985); New York, N.Y. BUS. CORP. LAW § 620(b)(McKinney Supp. 1980); North Carolina, N.C. GEN. STAT. § 55-73(b)(1962); Ohio, OHIO REV. CODE ANN. § 1701.591 (Anderson 1985); Pennsylvania, PA. STAT. ANN. tit. 15, §§ 1371-1381 (Purdon 1985); Rhode Island, R.I. GEN. LAWS § 7-1.1-51 (1969); South Carolina, S.C. CODE ANN. § 33-11-220 (Law Co. Op. Supp. 1984); Texas, TEX. BUS. CORP. ACT. ANN. art. 1201-12.54 (Vernon 1980 & Supp. 1984); Wisconsin, WIS. STAT. ANN. §§ 180.995(1)-(21)(West Supp. 1985). It is difficult to arrive at an exact count because of the great variety of statutes adopted by states dealing in varying degrees with close corporations. The criterion for selecting the laws appearing in the foregoing list is that each contains provisions specifically permitting deviations from the corporate norms and permitting partnershiplike planning among shareholders. Thus, these laws are comparable in their objective to 591.

²⁷ See *Statutory Close Corp. Supp. to the Mod. Bus. Corp. Act.*, 38 BUS. LAW. 1031 (1982). See also, *Proposed Statutory Close Corp. Supp. to the Model Bus. Corp. Act*, 37 BUS. LAW. 269 (1981). The reporter and principal draftsman of the MODEL ACT SUPPLEMENT was Professor Harry J. Haynsworth, whose article appears elsewhere in this symposium issue of the Law Review.

²⁸ See MODEL BUSINESS CORP. ACT ANN. § 35, at 756 (1977) (special comment — close corporations); Elfin, *A Critique of the Proposed Statutory Close Corporation Supplement to the Model Business Corporation Act*, 8 J. CORP. LAW 439, 441 (1983).

²⁹ See, e.g., MODEL ACT SUPPLEMENT § 21; DEL. CODE ANN. tit. 8 § 351 (1983).

³⁰ See e.g., MODEL ACT SUPPLEMENT § 20; ILL. ANN. STAT. § 1211. Shareholder protection provisions of this type will generally be hereinafter referred to as "management and control" provisions.

³¹ See, e.g., MODEL ACT SUPPLEMENT §§ 11-17; DEL. CODE ANN. tit. 8 § 202 (1983); N.J. REV. STAT. § 14A:7-12 (West 1969 & Supp. 1985); PA. STAT. ANN. tit. 15 § 372 (Purdon 1985).

³² See, e.g., MODEL ACT SUPPLEMENT § 40; N.J. REV. STAT. § 14A: 7-12 (West 1969 & Supp. 1985).

³³ Conceptually, there is an important difference between the thrust of the first three

One characteristic is shared by all the existing legislation. None of these laws is a self-contained law governing the close corporation exclusively and thereby fully displacing the general corporation law.³⁴ In other respects, however, the various close corporation statutory provisions differ greatly in form and in substance. Some are contained in a separate subchapter or supplement to the general corporation law, which deals with the subject matter in one place and in a comprehensive manner.³⁵ Others are scattered throughout the state's general corporation law.³⁶ The various laws are also quite different concerning the number of the four listed objectives covered, the comprehensiveness of their treatment of the subject matter, and the formalities required of the electing corporation.

The pioneering law, adopted by North Carolina in 1955,³⁷ had a major impact on the drafters of 591. So abbreviated and informal as almost to be overlooked among its counterparts in other states, it nevertheless embodies an approach that Ohio's drafters found appealing.³⁸

The Model Act Supplement, while taking the integrated subchapter approach of Delaware and other states, is considerably more comprehensive and innovative than any of the close corporation statutes that preceded it. Within its twenty-two sections, it covers in depth all four objectives of close corporation legislation. The Model Act Supplement can be expected to have considerable impact on the continuing enactment of special close corporation legislation, especially in those states that have taken no such action prior to its adoption.³⁹

objectives and that of the fourth. The first three objectives are all directed to encouraging advance planning on the part of the shareholders in order to simplify corporate governance and to avoid later friction among shareholders. The fourth objective is directed toward alleviating a breakdown in the shareholder relationship in the absence of effective advance planning. *See infra* text accompanying notes 191 - 95.

³⁴ D. VAGTS, BASIC CORPORATION LAW 779 (2d ed. 1979).

³⁵ These are generally referred to as the "integrated" close corporation laws. Examples include subchapter XIV of Delaware's corporation statute, one of the earliest integrated statutes, and the MODEL ACT SUPPLEMENT, which is the most recent prototype. Although far different than the other statutes in this category, 591 is also an integrated law, since it contains all of the special provisions dealing with close corporations. *See* MODEL ACT SUPPLEMENT at 1868 (comment to § 55).

³⁶ *See, e.g.*, CALIF. CORP. CODE § 158 (West 1980 Supp.); MINN. STAT. ANN. §§ 302A.201, .455, .457, .751 (West 1980).

³⁷ N.C. GEN. STAT. § 55-73(b)(1982).

³⁸ *See infra* note 82 and accompanying text.

³⁹ *See* Kessler, *The ABA Close Corporation Statute*, 36 MERCER L. REV. 661, 662 (1985); Solomon, *supra* note 13, at 304. In 1984, Wisconsin became the first (and thus far, the only) state to adopt, largely intact, the MODEL ACT SUPPLEMENT. WIS. STAT. ANN. §§ 180.995 (West Supp. 1985).

III. OTHER OGCL PROVISIONS AFFECTING CLOSE CORPORATIONS

A number of other sections of the OGCL, which antedated 591, are of special significance to the close corporation. Most of these provisions, interspersed throughout the OGCL and applicable to all Ohio corporations, were no doubt designed for close corporation use.⁴⁰ Although 591 has become the key provision of Ohio law dealing with close corporations, these other sections and their continuing role must be part of a complete assessment of the position of the close corporation under Ohio law.

The effect of these sections can best be appreciated by examining them in terms of whether their impact on the close corporation lies in the area of procedure or substance. First then, in the category of simplifying corporate procedures, are provisions permitting: the use of only one person as incorporator;⁴¹ reductions of the standard minimum of three directors to one director if there is only one shareholder, or to two directors if there are only two shareholders;⁴² action by either shareholders or directors by unanimous written consent in lieu of a meeting;⁴³ and telephonic meetings of directors.⁴⁴

Next, in the category of substance, it is helpful to subdivide the provisions into self-executing and enabling types.⁴⁵ The self-executing items consist of provisions mandating: pre-emptive rights for shareholders;⁴⁶ cumulative voting for the election and against removal of directors;⁴⁷ a shareholder's right of inspection of corporate records for reason-

⁴⁰ See O'Neal, *supra* note 25, at 878-79.

⁴¹ O.R.C. § 1701.04.

⁴² O.R.C. § 1701.56. Illinois' new Business Corporation Act allows the board of directors to consist of one or more members, regardless of the number of shareholders. ILL. ANN. STAT. ch. 32, (P) 8.10 (Smith-Hurd 1985).

⁴³ O.R.C. § 1701.54. Since 1981, Minnesota law has permitted the articles of incorporation to authorize the taking of action by a writing signed by only the number of directors required to take the same action at a meeting, provided that all directors are notified immediately following. MINN. STAT. ANN. § 302A.239 (West 1985).

⁴⁴ O.R.C. § 1701.61(B).

⁴⁵ The distinction between "self-executing" and "enabling" legislation appears repeatedly throughout this article and is critical to an understanding of a number of positions taken. Self-executing legislation imposes rules of conduct that are automatically effective with regard to a corporation without the necessity of any action on the part of the corporation or its shareholders. Enabling (or "permissive") legislation, on the other hand, merely provides the opportunity for the corporation and its shareholders to take action to adopt rules of conduct. See WEBSTER'S NEW UNIVERSAL UNABRIDGED DICTIONARY 596, 1646 (2d ed. 1983); Kessler, *supra* note 39, at 697.

⁴⁶ O.R.C. § 1701.15. This section permits the total elimination of pre-emptive rights by a provision in the articles of incorporation. In addition, it contains a number of exceptions, including one for treasury shares. Compare O.R.C. § 1701.591(C)(10); see *infra* text accompanying note 129.

⁴⁷ O.R.C. § 1701.55. Ohio Senate Bill No. 259, 116th Gen. Assembly, Gen. Sess. 1986, Ohio Legis. Serv. 5-278 (Baldwin), which became effective July 24, 1986, amended O.R.C.

able and proper purposes;⁴⁸ a shareholder's right to an annual financial statement;⁴⁹ the holding of an annual meeting of shareholders;⁵⁰ and dissenters' rights of appraisal upon the occurrence of fundamental changes involving the corporation or its business.⁵¹

The items authorized by enabling provisions consist of:⁵² voting trusts and irrevocable proxies;⁵³ classification of shares and voting by classes;⁵⁴ classification of directors;⁵⁵ high percentage quorum and voting require-

§ 1701.55 and other sections of the OGCL to permit the elimination of cumulative voting rights by (and only by) the adoption of an amendment to the articles of incorporation. The new amendment provisions do, however, incorporate safeguards applicable to close corporations. They provide that, unless the corporation's shares are publicly traded, adoption of the necessary amendment can be defeated by the votes of a number of shares that if voted cumulatively, would be sufficient to elect at least one director. In addition, action to adopt the amendment must be preceded by written notice to shareholders that conspicuously warns of the adverse consequences of the amendment to minority shareholders. No amendment can be adopted on behalf of a close corporation earlier than ninety days after the formation of the corporation.

Earlier versions of the bill had exempted from the ninety day requirement a corporation for which cumulative voting had been eliminated "pursuant to section 1701.591." Such language, however, was dropped from the final form of the bill as being unnecessary, since the elimination of cumulative voting rights is clearly permitted under a close corporation agreement adopted pursuant to 591. See *infra* note 113. None of the formalities specified under Senate Bill 259 is required for elimination of cumulative voting pursuant to a close corporation agreement. Should the agreement be later terminated, however, cumulative voting rights would be reinstated and could not be denied to a minority shareholder except by the adoption of an amendment to the articles that complies with the requirements imposed by Senate Bill 259.

At first blush, providing the ability to opt-out of cumulative voting might appear to be a serious diminution of already sparse self-executing protection provided by Ohio law for minority shareholders. See *infra* text accompanying note 209. On the other hand, the benefits of being a minority director may, except for its watchdog function, be more apparent than real. See *supra* note 14, 37 Cin. L. Rev. at 626-27. Certainly, whatever benefit a minority shareholder might achieve through cumulative voting would be slight in comparison to the more concrete protection of individual rights available to him under a specially tailored close corporation agreement. In order to deprive the minority of cumulative voting rights, the majority, whether it proceeds through the use of an amendment to the articles or a close corporation agreement, will have to deal with the minority in order to achieve its purpose. Thus, either event will present an opportunity for constructive discussion and bargaining between the shareholder factions covering all aspects of their relationship.

⁴⁸ O.R.C. § 1701.37(C). In contrast, 591(C)(9) affords an unrestricted right of inspection. See *infra* note 134 and accompanying text.

⁴⁹ O.R.C. § 1701.38.

⁵⁰ O.R.C. § 1701.39. See *infra* notes 172-76 and accompanying text for a discussion of a recommended amendment to permit the relaxation of this requirement.

⁵¹ O.R.C. § 1701.85.

⁵² The OGCL sections listed in notes 54-58 require that the special requirement be contained in the articles of incorporation.

⁵³ O.R.C. §§ 1701.49, 1701.48.

⁵⁴ O.R.C. §§ 1701.04, 1701.06.

⁵⁵ O.R.C. § 1701.57.

ments for shareholder and director meetings;⁵⁶ voluntary dissolution by a vote of less than a majority;⁵⁷ and appointment of a provisional director where necessary to break a deadlock in the board of directors.⁵⁸

These provisions of the OGCL, like their counterparts in the corporation laws of other states, are highly inadequate to deal with the special needs of the close corporation. Their main accomplishment is to loosen, somewhat, the procedural straightjacket by permitting a degree of informality in the conduct of internal affairs. In, however the vastly more important substantive area of management and control, they meet the close corporation's needs only to a severely limited extent, and even then at a high and often prohibitive cost in terms of complicated drafting requirements, substantial legal fees and uncertainty as to enforceability.⁵⁹ Still, their greatest shortcoming is the complete inability to make available certain far more effective planning devices possible under 591.⁶⁰

The final subject to be addressed in this segment is the remaining significance of these other OGCL provisions, now that 591 is on the books. The procedural and the *self-executing* substantive provisions, since they have automatic application, continue to have vitality, especially where no steps to engage in close corporation planning are taken by the shareholders. However, the opposite is true of the *enabling* substantive provisions, which, like 591, can be availed of only by the taking of affirmative steps by the shareholders. It is chiefly here that, as proclaimed in the lyrics of that popular song from the hit Broadway musical play of the 40's, 591's boast to the rest of the OGCL can legitimately be: "Anything you can do, I can do better; I can do anything better than you."⁶¹ Because the subject matter can now be treated so much more effectively and economically by a close corporation agreement, it must be recognized that these older planning provisions of the OGCL have been rendered obsolete by 591.⁶²

⁵⁶ O.R.C. §§ 1701.51, 1701.52, 1701.62. Cf. 591(C)(3) ("voting requirements need not appear in the articles unless the close corporation argument is set forth in the articles.")

⁵⁷ O.R.C. § 1701.86(E). Cf. 591(C)(2)(close corporation agreement may provide for dissolution by one or more shareholders).

⁵⁸ O.R.C. § 1701.911. For a qualitative comparison of this remedy with the use of arbitration, which may be availed of pursuant to a provision contained in a close corporation agreement pursuant to 591(C)(11), see *infra* note 135.

⁵⁹ Ginsberg, *supra* note 14, at 9. See *infra* notes 136, 137 and accompanying text. See MODEL ACT SUPPLEMENT at 1806 (introductory comment).

⁶⁰ See *infra* notes 138-40 and accompanying text.

⁶¹ Berlin, "Anything You Can Do," from "Annie Get Your Gun" (1946).

⁶² The distinction that a close corporation agreement requires shareholder unanimity and the other OGCL provisions discussed do not is unimportant. As a practical matter, the subject of the planning action will be such that, regardless of the means used, it will be necessary that all shareholders concur. This is so because the planning will almost always

In every case, therefore, where clients are engaged in close corporation planning, counsel should seriously consider the use of a close corporation agreement as the means of accomplishing the clients' objectives.⁶³ Moreover, except where only the simplest type of planning is desired by the clients, a close corporation agreement should be the vehicle.⁶⁴

IV. "LEGISLATIVE HISTORY"⁶⁵ OF 591

The Ohio General Assembly passed 591 on November 17, 1981, and it became effective the same day.⁶⁶ The law was amended in a number of

be directed to protective measures for minority shareholders or delineation of the rights of two sole equal shareholders.

⁶³ Throughout this article the emphasis is on the value of a close corporation agreement as a comprehensive planning tool in the organizational stage of the corporation. It should not be overlooked, however, that 591 can provide the means to structure a direct and simplified solution to a special problem of narrow scope confronting the shareholders of an existing corporation.

⁶⁴ Serious implications regarding legal ethics and malpractice may be present when an attorney undertakes the organization of a close corporation having more than one shareholder. Problems may arise where the attorney represents both majority and minority shareholders or, perhaps, even where the formal representation is confined to a majority shareholder, when the minority shareholder is not represented by other counsel. See O'Neal and Thompson, *supra* note 19, at vii, § 9:02. The preparation of a close corporation agreement under these circumstances raises questions relating to conflict of interest and duties incumbent upon a lawyer acting as "intermediary." See J. Lewis and A. Cirulnick, *Stockholders' Agreements*, 20 A.L.I./A.B.A. COURSE MATERIALS JOURNAL (No. 1) 49, 51-54 (1985); Weinberg, *New Close Corporation Law: A Green Light and a Yellow Light for Ohio Lawyers*, 55 OHIO ST. B. ASS'N REP. 1068, 1068-70 (1982); Karjala, *A Second Look at Special Close Corporation Legislation*, 58 TEX. L. REV. 1207, 1228 (1980). An effect of the greatly facilitated planning option made possible by 591 may well be to intensify these problems.

⁶⁵ The author has appropriated the phrase for the title of this section of the article, since no meaningful legislative history is maintained by the Ohio General Assembly with respect to its proceedings. The only official publications of the activities of the General Assembly are the "Journals of the Senate and House of Representatives." The Journals, pursuant to Article II, § 15(C) of the Ohio Constitution, record, in the nature of a docket, the earlier readings and final vote on bills on the floor of the House of Representatives and Senate. There is no record kept of testimony, statements, or debate, either in committee or on the floor of either House.

⁶⁶ Following final action on Amended Ohio House Bill No. 455, 114th Gen. Assembly Gen. Sess. (1981), Ohio Legis. Serv. 5-593 (Baldwin), by the General Assembly, it was signed the same evening by Governor James Rhodes. The Bill became effective immediately by virtue of an emergency clause. The author would like to believe that the politicians were in agreement with the academicians that the need for remedial close corporation legislation was so great that emergency action was warranted. One need not be a cynic, however, to suspect that such was not the case. Instead, the Corporation Law Committee's uncontroversial (the bill passed the Ohio House by an 87-0 vote) child happened to have toddled into the Senate at the opportune time for the politicians to make it the subject of a logrolling type of exercise by adding to HB 455 urgent action to protect Marathon Oil Co. against the pending takeover bid of Mobil Oil Co. The result was the addition to the original close corporation law bill of a new unrelated section, O.R.C. § 1331.021, dealing with the

respects, effective April 4, 1985.⁶⁷ The amendments were chiefly of a technical nature.⁶⁸ There were several language clarifications,⁶⁹ and a few minor substantive changes.⁷⁰

A retroactivity provision with respect to the 1985 amendments is contained in division (N). Discussions among the Close Corporation Subcommittee, counsel for the Senate Judiciary Committee, and representatives of the Ohio Legislative Service Commission took place regarding retroactivity during the early stages of the legislation. All were in agreement on the desirability of making the amendments retroactive, so as to encompass all close corporation agreements entered into since the original enactment of 591 in 1981.⁷¹ That is clearly the intent of division (N), although there is technical inaccuracy in the language used, since the reference is to "close corporations created on or after November 17, 1981" rather than, as it should have been, to "close corporation agreements adopted" after that date.⁷²

Since close corporation agreements are treated the same under 591 regardless of whether they were entered before or after the various amendments, the discussion of the provisions of 591 below⁷³ will be addressed to the law as amended to the date of this article, with no distinction between the original and amended versions of the law.

evils of "reducing competition in the sale of petroleum products in Ohio" and including an emergency clause providing for immediate implementation of the expanded act. See Lorincz, *U.S. Steel Finds Gusher in Ohio*, N. OHIO BUS. J. 3 (Nov. 23, 1981).

⁶⁷ Amended substitute Ohio House Bill 607, 115th Gen. Assembly, Gen. Sess. (1984), Ohio Legis. Serv. 5-895 (Baldwin) signed by Governor Richard Celeste on January 3, 1985. When Chapter 1308 of the Ohio Revised Code was amended in 1983 for the purpose of authorizing the issuance of shares in uncertificated form, division (M) was added to 591 to bar the use of uncertificated securities by any corporation that is the subject of a close corporation agreement. An inconsequential conforming amendment to division (C)(7) of 591 occurred also in 1984 when the language of O.R.C. § 1701.33 concerning the declaration of dividends was expanded to include "distributions." See OHIO GENERAL CORPORATION LAW 63,94 (Judson-Brooks ed. 1986) ("Committee Comment (1984)" to O.R.C. §§ 1701.33, 1701.591).

⁶⁸ See *Report of the Corporation Law Committee*, 57 OHIO ST. B. ASS'N REP. 498 (1984); OHIO GENERAL CORPORATION LAW 94 (Judson-Brooks ed. 1985) "Committee Comment (1985)" to 591.

⁶⁹ The most important clarification is discussed in *infra* note 113.

⁷⁰ See *infra* notes 104 and 106.

⁷¹ Correspondence and notes received and compiled by the author in his capacity as Chairman of the Close Corporation Subcommittee of the Corporation Law Committee of the Ohio State Bar Association.

⁷² The official heading of 591 is "Close Corporation Agreements" and the entire emphasis of the section is on the agreement. Thus, there is no such thing as a statutory "close corporation" in Ohio; there is only a statutory "close corporation agreement."

⁷³ See *infra* text under the heading "Explanation of 591."

V. OBJECTIVE, PHILOSOPHY, AND APPROACH OF 591

The objective of 591 is to provide the means for shareholders of Ohio close corporations to take foolproof action to (1) free themselves and the corporation of standard corporate formalities, and (2) engage in advance planning for the purpose of arranging their relationship *inter se* as if they were members of a partnership.⁷⁴ The philosophy underlying 591 is the accomplishment of its objective in the simplest manner possible.⁷⁵ The law's approach is the use, as in the case of a partnership, of a straightforward agreement as the sole vehicle to achieve the objective.⁷⁶

The drafters of 591 were aware that, compared to the broadest possible scope of special close corporation legislation,⁷⁷ theirs was a narrow objective. Their assignment⁷⁸ was limited to insuring freedom of contract to shareholders seeking informality and the arrangement of their internal affairs in partnershiplike fashion.⁷⁹ An important related objective, however, was to formulate a law that, by its nature, would encourage its widespread use by lawyers engaged in the general practice, as well as by corporation specialists.

The drafters believed that, consistent with their objectives of making it possible to simplify the corporate form, the means of accomplishing their objective should likewise be as uncomplicated and direct as possible.⁸⁰ They were convinced that the comparable laws of most other states were needlessly complex and that, mainly for that reason, they were not meeting with wide acceptance.⁸¹ Yet, at the other extreme, the highly

⁷⁴ See Report of the Corporation Law Committee, 53 OHIO ST. B. ASS'N REP. 510, 516 (1980).

⁷⁵ *Id.* at 510.

⁷⁶ *Id.* at 516.

⁷⁷ See *supra* text and accompanying notes 29-33.

⁷⁸ For information concerning the deliberations of the committees responsible for the drafting of 591, see *infra* note 163.

⁷⁹ Validation of the agreement establishing the relationship among shareholders is the heart of special close corporation legislation. See Johnson, *The Texas Close Corporation Law: Some Observations and Modest Proposals*, 15 TEX. TECH. L. REV. 779, 794 (1984); Kessler, *supra* note 39, at 676. As the preventative aspect of such legislation, it serves a purpose that is independent of the remaining major aspect, which is a self-executing provision embodying remedies for shareholder oppression. See *infra* text under heading "Need for Additional Legislation - Relief of Shareholder Oppression."

⁸⁰ See Mann, *supra* note 18, at 292, 341. It might be noted that the creation of simplified legislation is a goal worthy of guiding the efforts of draftsmen in all areas of the law. See Bok, *A Flawed System of Law Practices and Training*, 33 J. LEGAL EDUC. 570, 583 (1983).

⁸¹ See Committee On Corporate Laws, *Proposed Statutory Close Corp. Supplement To The Model Business Corp. Act*, 37 BUS. LAW 269, 272 (1981); Kessler, *supra* note 39, at 670; Hetherington & Dooley, *Illiquidity and Exploitations: A Proposed Statutory Solution to the Remaining Close Corporation Problem*, 63 VA. L. REV. 1, 60-61 (1977). This has been recognized as a major reason for the repeal of the initial close corporation law adopted by the State of Texas, TEX. BUS. CORP. ACT ANN. art. 2.30-1 to -5 (Vernon 1980) and enactment of

abbreviated and negative approach of the North Carolina statute seemed to be dangerously ill-equipped to accomplish the demanding task of unequivocally bringing about such a radical change in the established law.⁸² Consequently, the decision was made that Ohio's statute should take a different tack.

The approach of 591 is to require, in order to enjoy the advantages provided by the law, only the single step of signing a qualified close corporation agreement. Nevertheless, in sharp contrast to the few states employing the same simple technique,⁸³ 591 provides strong assurance of the durability of the agreement through detailed provisions pointedly designed to overcome any claim of invalidity founded on inconsistent, deep-rooted corporate doctrine.⁸⁴

A key factor in 591's simplified approach is the absence of a requirement that an election of close corporation status appear in the articles of incorporation.⁸⁵ Likewise, no provision of the close corporation agreement need be set forth or referenced in the articles; this is true no matter how radical the departure from the corporate norm, such as, for example, elimination of the board of directors. The role of the statute is likewise limited. Its sole function is to legitimize the agreement, define the boundaries of its permitted subject matter, and prescribe the requirements for its creation and continued effectiveness.⁸⁶ Beyond that, 591

its successor law, TEX. BUS. CORP. ACT ANN. art. 12.01.54 (Vernon 1981); Blunk, *Analyzing Texas Articles of Incorporation: Is the Statutory Close Corporation Format Viable?* 34 SW. L.J. 941, 942 (1980); Johnson, *supra* note 79, at 780, 781.

⁸² N.C. GEN. STAT. § 55-73(b)(1982). This statute, consisting of little more than a dozen lines, simply provides that no agreement among all shareholders relating to any phase of the affairs of the corporation shall be invalid as between the parties on the ground that it is an attempt to treat the corporation as if it were a partnership. Cf. 591(F)(1)(parallel Ohio close corporation provisions). Paragraph (c) of the same North Carolina statutory section consumes only a few additional lines in stating that an agreement among all or less than all shareholders is not invalid on the ground that it interferes with the discretion of the board of directors. Cf. 591(F)(3)(parallel Ohio close corporation provisions). For a discussion of the uncertainty resulting from the negative phrasing of statutory close corporation provisions, see Wang, *The California Statutory Close Corporation: Gateway to Flexibility or Trap for the Unwary?*, 15 SAN DIEGO L. REV. 687, 704-05 (1978)(concerning CALIF. CORP. CODE § 300(b) which is modeled on the North Carolina statute).

⁸³ FLA. STAT. § 607.107(2); GA. CODE ANN. § 14-2-120(b); N.C. GEN. STAT. § 55-73(b) & (c). The Florida and Georgia laws are in substance and length very similar to the North Carolina statute.

⁸⁴ See Bradley, *A Comparative Evaluation of the Delaware and Maryland Close Corporation Statutes*, 1968 DUKE L. J. 525, 527 (1968).

⁸⁵ 591(A)(2) does provide the option of placing the entire close corporation agreement in the articles of incorporation or code of regulations rather than in a "written instrument." As to the advisability of including the agreement in the articles or, instead, in a separate writing, see *infra* note 126 and accompanying text. For a form of single shareholder close corporation agreement contained in the articles, see Appendix B.

⁸⁶ 591(A), (C), (I).

itself adds nothing to the special features of the corporation or the special relationship among its shareholders. Instead, these must, in their entirety, be created and contained in the agreement.

The broad test selected for the corporation's eligibility under 591 is the absence of a public market for the trading of the corporation's stock,⁸⁷ rather than the arbitrary and more restrictive test of an upper limit on the number of shareholders.⁸⁸ Finally, eligibility does not require that there be restrictions on the transfer of the stockholders' shares.⁸⁹

In opting for the exclusivity of the agreement, the drafters departed from a fundamental principle of corporation law, which has been followed in the close corporation legislation of most other states. These laws require that the election of close corporation status and the adoption of radical departures from the corporate norm be set forth in the charter document.⁹⁰ Taking into consideration the purposes of special close corporation legislation, as well as the legitimate interests of all affected parties, there appears to be no justification for making special charter provisions a prerequisite to special close corporation status.⁹¹ In some

⁸⁷ See *infra* text accompanying note 98.

⁸⁸ The following are examples of the more restrictive test: thirty in Delaware, DEL. CODE ANN. tit. 8, § 342 (1983); thirty in Pennsylvania, PA. STAT. ANN. tit. 15, § 1372 A.1 (Purdon Supp. 1986); twenty in Maine, ME. REV. STAT. ANN. tit. 13-A, § 102.5 (1981); and thirty-five in California (increased from ten as contained in the original 1975 statute), CAL. CORP. CODE § 158(a) (West 1986). The test in the MODEL ACT SUPPLEMENT § 3(b), although numerical, takes a novel approach. It requires that the corporation have no more than fifty shareholders at the time of its election, but termination of close corporation status can occur only by shareholder action revoking it. Thus, an increase of the number of shareholders beyond fifty, or even a public share offering will not result in the loss of close corporation status. See MODEL ACT SUPPLEMENT, *supra* note 27, at 1811 (Official Comment to § 3).

⁸⁹ Restrictions on transfer are required for eligibility in most other close corporation statutes. See, e.g., DEL. CODE ANN. tit. 8, § 342(a)(2) (1983); MD. CORPS & ASS'NS CODE ANN. § 4-503 (1985). In most instances, restrictions on the transfer of shares will be an indispensable element of sound close corporation planning. See *infra* text under heading "Need for Additional Legislation - Share Transfer Restrictions." A form of multi-shareholder close corporation agreement is contained in Appendix C. However, the drafters concluded that it was unwise to deny the use of 591 to an otherwise eligible corporation whose shareholders, for their own special reason, choose not to impose restrictions on transfer. See Karjala, *supra* note 64, at 1257.

⁹⁰ See, e.g., MODEL BUSINESS CORP. ACT SUPP. § 10 (1985); DEL. CODE ANN. tit. 8 § 351 (1983); MICH. COMP. LAWS § 450.1463 (1986).

⁹¹ See Bradley, *supra* note 84, at 553; Kessler, *supra* note 39, at 670-73; O'Neal, *Close Corporations: Existing Legislation and Recommended Reform*, 33 BUS. LAW 873, 880 (1978). In addition, recent New York decisions cast serious doubt on the effectiveness of requiring charter provisions. They have held that an agreement among all shareholders is enforceable in spite of the failure of the corporate charter to include the disputed provisions as mandated by the applicable statute. *Adler v. Svingos*, 80 A.D.2d 764, 436 N.Y.S.2d 719 (1981) (New York law applied); *Zion v. Kurtz*, 50 N.Y.2d 92, 405 N.E.2d 681, 428 N.Y.S.2d 199 (1980) (a four to three decision applying Delaware law).

The illogic of requiring charter provisions is demonstrated by the partnership analogy.

instances, third parties dealing with the corporation will want to ascertain whether or not a close corporation agreement is in existence. However, in lieu of an examination of the articles of incorporation for that purpose, they can just as effectively, by the exercise of diligence, make that determination in other ways.⁹² Present and future shareholders of the corporation likewise stand to gain no unique protection from special charter provisions.⁹³ Under 591, the former are protected by the requirement of unanimous shareholder participation in the close corporation agreement,⁹⁴ and the latter by the requirement that all stock certificates bear a legend indicating the enterprise's close corporation status.⁹⁵

VI. EXPLANATION OF 591

As emphasized above, 591's sole purpose is to validate and provide the ground rules governing a close corporation agreement among the corporation's shareholders. Although the section is fairly lengthy and consists of fourteen divisions,⁹⁶ it accomplishes no more and no less than that.

This portion of the article focuses on the specific provisions of 591. Rather than treating each division of 591 in its alphabetical order, the following is a functional approach to an analysis of the statute.

Public recording is a concept foreign to partnership law, except in the case of a limited partnership, where the requirement of filing a certificate is for the purpose of alerting third parties to the reduced financial commitment of the limited partners. REVISED UNIFORM LIMITED PARTNERSHIP ACT § 201 Comment, 6 Uniform Laws Ann. (1985 Supp.). In contrast, practically any person dealing with a corporation is aware that he or she is looking solely to the corporate assets, and this remains true regardless of whether or not it is a regular corporation or a statutory close corporation. Thus, aspects of the internal relationship among shareholders and matter of corporate governance are irrelevant to the rights of creditors and other third parties. See Kessler, *supra* note 39, at 696. Professor Kessler is also critical of the required bifurcation of provisions between the agreement and the charter, as being unnecessary, confusing, and a possible trap for the unwary. Kessler, *supra* note 39, at 697, 699. It should be pointed out, in addition, that the result of many of the laws is an even more complicated trifurcation of provisions governing the ongoing affairs of the corporation among the agreement, the charter document, and sections of the statute itself. See, e.g., MODEL ACT SUPPLEMENT §§ 11-15; M.D. CORPS. & ASS'NS CODE ANN. § 4-404 (1985).

⁹² See Karjala, *supra* note 64, at 1262. 591(B) was added by the 1985 amendments for the purpose of providing added protection to third parties dealing with the corporation. See *infra* note 104 and accompanying text.

⁹³ O.R.C. § 1701.08(B), provides that no person dealing with an Ohio corporation is charged with constructive notice of the contents of its filed articles of incorporation.

⁹⁴ 591(A)(1). See Kessler, *supra* note 39, at 672.

⁹⁵ 591(H). See Kessler, *supra* note 39, at 672. If there is a failure to denote the existence of a close corporation agreement by a legend on the stock certificate and, as a result, someone purchases the stock without knowledge of the close corporation agreement, the agreement becomes invalid under 591(I). See *infra* text accompanying note 106.

⁹⁶ As stressed above, great pains were taken to assure that the statute is not complicated. Practically all of the operative provisions are contained in divisions (A) and (C).

A. Eligibility, Formalities, and Termination

Any Ohio corporation organized for profit,⁹⁷ regardless of the number of its shareholders, may be the subject of a close corporation agreement, unless its shares are listed on a national securities exchange or are regularly quoted in the over-the-counter market.⁹⁸ The subsequent occurrence of such listing or quotation will invalidate the agreement.⁹⁹ An agreement qualifies under 591 if (1) all of the shareholders, whether owning voting or nonvoting stock, assent to it,¹⁰⁰ (2) the agreement is set forth in the articles of incorporation, code of regulations or another written instrument, and (3) the agreement states that it is to be governed by 591.¹⁰¹ Because there must be unanimous assent of shareholders, as a practical matter, corporations with many shareholders, although technically eligible if their shares are not publicly traded, will be unable to qualify under 591.¹⁰²

There are few required formalities. In addition to the agreement itself, it is necessary that the stock certificates bear a legend indicating the existence of the agreement¹⁰³ and that an agreement not set forth in the articles or the regulations be entered in the minutes of the shareholders.¹⁰⁴ The failure to comply with either of these two requirements will

⁹⁷ Professional corporations governed by O.R.C. Chapter 1785 are among the most likely candidates for a close corporation agreement, since, by their nature, especially the active participation of all shareholders, they invariably are the classic close corporation. See *supra* text accompanying notes 12 and 13. See Z. & M. CAVITCH, OHIO CORPORATION LAW WITH FEDERAL TAX ANALYSIS § 2.19 [7][e] (1986).

⁹⁸ 591(I).

⁹⁹ *Id.*

¹⁰⁰ The corporation itself need not be a party to the agreement in order to be bound by it. Any doubt as to this was removed by the 1985 amendments, which added to the introductory paragraph of 591(C) the dependent clause "which shall be binding on the corporation and all of its shareholders. . . ." It is, however, advisable to include the corporation as a party in order to retain maximum residual effectiveness of the agreement in the event of its subsequent non-consensual termination. See *infra* text under heading "Explanation of 591-Savings Clause." See also Z. & M. CAVITCH *supra* note 97, at § 2.19 [7][e].

¹⁰¹ 591(A). See also O.R.C. § 1701.01(x), for the definition of "close corporation agreement," which is merely a reference to the three requirements of 591(A).

¹⁰² See OHIO GENERAL CORPORATION LAW 93 (Judson-Brooks ed. 1986) ("Committee Comment (1981)" to 591); N.Y. BUS. CORP. LAW § 620 (McKinney Supp. 1980)(Comment); Johnson, *supra* note 79, at 794.

¹⁰³ 591(H).

¹⁰⁴ 591(B). This provision was added by the 1985 amendments. Its purpose is to facilitate the corporation's dealings with third parties. The effect, under O.R.C. § 1701.92(c), of entering a close corporation agreement in the minutes is to make a copy of it, which is certified by the secretary or assistant secretary, conclusive in favor of a nonshareholder who has relied on it in good faith. Like treatment would be accorded the officer's certification that no close corporation agreement is in effect.

not invalidate the close corporation agreement.¹⁰⁵ Invalidation could later occur, however, as a result of the transfer of a stock certificate bearing no legend to a person who takes other than by gift, bequest, or inheritance and without knowledge of the agreement.¹⁰⁶ A transferee of share certificates bearing a legend is conclusively deemed to have taken delivery with notice of the agreement and is bound by it.¹⁰⁷ In keeping with the legend requirement, a corporation having a close corporation agreement in effect may not issue shares in uncertificated form,¹⁰⁸ as otherwise permitted by Ohio law.¹⁰⁹

Action to amend or terminate a close corporation agreement can be taken by a four-fifths vote of the shares of each class, unless the agreement requires a greater percentage of any class.¹¹⁰

¹⁰⁵ A failure to file the agreement with the minutes is specifically covered by 591(F)(4), but there is no provision dealing with the effect of a failure to legend the stock certificates. The clear implication of division (I), however, is that there is no impact of such latter failure unless followed by an invalidating transfer.

¹⁰⁶ 591(I). This division provides that invalidation occurs subsequent to any such transfer, if the transferee does not consent in writing to the close corporation agreement within thirty days after issuance of a stock certificate in the name of the transferee or his nominee. The event in the original law that triggered the beginning of the thirty-day period was receipt by the transferee of a copy of the close corporation agreement. It was changed by the 1985 amendments to issuance of a stock certificate in the transferee's name. In addition, the amendments added the obligation of an officer, who learns of invalidity, to notify all shareholders immediately. See OHIO GENERAL CORPORATION LAW 94 (Judson-Brooks ed. 1986) ("Committee Comment (1985)" to 591). If the invalid agreement appears in the articles of incorporation, it is required that action be taken to file a certificate of amendment to the articles deleting the agreement. Invalidation of the agreement does not necessarily mean that none of its provisions will remain enforceable. Instead, there will be voided only those provisions that would be illegal under Ohio law absent the sanction provided by 591. See *infra* text under the heading "Explanation of 591-Savings Clause."

¹⁰⁷ 591(H).

¹⁰⁸ 591(M).

¹⁰⁹ O.R.C. § 1701.24(F).

¹¹⁰ 591(E). Obviously, in order to gain lasting protection, a shareholder owning twenty percent or less of the stock must make sure that the agreement contains a provision increasing the size of the majority vote required to amend or terminate to the extent necessary to give the shareholder a veto. For the recommendation that 591(E) be amended to provide that the vote to amend or terminate a close corporation agreement be increased to one hundred percent, see *infra* text under heading "Need for Additional Legislation-Improving 591."

B. *What Can Be Accomplished by a Close Corporation Agreement*¹¹¹

Division (C) is the heart of 591, in that it specifies in depth the permissible subject matter of a close corporation agreement.¹¹²

The key language is contained in the opening paragraph of 591(C), which permits the agreement, "[i]rrespective of any other provisions of [the OGCL],"¹¹³ to regulate "any aspect of the internal affairs of the corporation or the relations of the shareholders among themselves. . . ." The effect of this broad, yet clearly defined, grant of authority is that, except for precise narrow limitations set forth in division (D),¹¹⁴ the sky is the limit regarding the corporation's internal affairs and the shareholders' relations *inter se*, but that provisions attempting to affect the rights of third parties are out of bounds. The full scope of the subject matter authorized for inclusion in the agreement is better appreciated when division (C) is considered together with division (F) of 591. The latter rules out attacks on the agreement on grounds that it departs from corporate norms or treats the corporation as if it were a partnership.¹¹⁵ The agreement's grant of authority under division (C) encompasses both procedural matters designed to simplify the structure and operation of

¹¹¹ The reader is cautioned that certain provisions of a close corporation agreement could adversely affect the status of the corporation as an S corporation under Subchapter S of the Internal Revenue Code. The danger lies in the requirement under I.R.C. § 1361(b)(1)(D) that a corporation, in order to be eligible for Subchapter S treatment, not have more than a single outstanding class of stock. Differences in the rights adhering to stock held by parties to the agreement might be considered to create a disqualifying second class of stock. I.R.C. § 1361(c)(4) provides that a difference among shareholders in voting rights will not give rise to more than one class. However, differences in regard to the distribution of profits or assets may result in the Internal Revenue Service asserting the existence of a second class. See Z. & M. CAVITCH, *supra* note 97, at § 2.19[7][a]; D. SCHENK, *FEDERAL TAXATION OF S CORPORATIONS* § 404 (1985). At the other extreme, there would appear to be no danger in the Sixth Judicial Circuit that the existence of a close corporation agreement would jeopardize the corporation's right to be taxed as a corporation under the Internal Revenue Code. See Z. & M. CAVITCH, *supra* note 97 at § 2.19[7][b]. See also, Wang, *supra* note 82, at 717-27 (thorough discussion of federal tax problems that might result from the adoption of a "shareholders' agreement" pursuant to § 300(b) of California's close corporation provisions).

¹¹² This is 591's most significant point of departure from the scheme of the pioneering North Carolina statute. See *supra* note 82 and accompanying text.

¹¹³ The addition of the "irrespective" clause was the most important of the clarifications effected by the 1985 amendments. The clause is intended to remove any doubt that an agreement adopted in accordance with the requirements of division (A) of 591 and within the scope specified in division (C) can override any other provision of the OGCL, except the "untouchable" sections listed in division (D). The clause had appeared in earlier drafts of the original law, but was inadvertently dropped prior to its introduction in the General Assembly.

¹¹⁴ See *infra* text under the heading "Explanation of 591-Express Limitation on the Scope of a Close Corporation Agreement."

¹¹⁵ See *infra* text under the heading "Explanation of 591-Negation of Traditional Obstacles."

corporate governance and substantive matters dealing with management and control.¹¹⁶

Following its broad opening paragraph, division (C) contains a "laundry list" of eleven items that are included in the broad grant. The laundry list is a comprehensive catalog, culled from the close corporation statutes of various states, of specific items sanctioned for agreement among shareholders. It does not, of course, limit the scope of the grant.¹¹⁷ The laundry list has two purposes. One is the express statutory recognition of the legitimacy of these traditionally sensitive topics for inclusion in a close corporation agreement.¹¹⁸ The other serves the practical function of alerting counsel to a list of the more prominent areas to explore with clients, who wish to form a close corporation.¹¹⁹

While again stressing that there are few internal matters that cannot, pursuant to the opening paragraph of division (C), be the subject of a close corporation agreement, attention is next directed to specific items of the laundry list.

Perhaps the most revolutionary of the group, and one that has become a hallmark of modern close corporation legislation, is the ability to eliminate the board of directors.¹²⁰ The result of such action is that the shareholders are deemed to be the directors to the extent not inconsistent with the agreement, and that they succeed to the rights and liabilities of directors.¹²¹ This same item of the laundry list also permits a lesser

¹¹⁶ Procedural and substantive matters frequently overlap when control and management are involved. For example, elimination of the board of directors necessarily involves the determination by the shareholders of the persons on whom authority will be conferred to fill the vacuum.

¹¹⁷ An early draft of the statute contained that venerable redundancy "including, but not limited to" preceding the laundry list. However, the Ohio Legislative Service Commission, which must approve the form of all bills introduced in the Ohio General Assembly, commendably disapproved the use of "but not limited to" as being unnecessary and undesirable. The Maryland legislature is on record as being in accord. MD. CORPS. & ASS'NS CODE ANN. § 4-401 (1985)(Revisor's Note).

¹¹⁸ See *supra* text accompanying notes 82-84.

¹¹⁹ A checklist of this type adds an educational function to the statute. Recent corporation laws indicate a possible trend in this direction. See MINN. STAT. ANN. § 302A.111 (West 1985)(Reporter's Notes)(cited in Note, *Minnesota Business Corporations Act: Greater Freedom for Corporations*, 66 MINN. L. REV. 1022, 1034-35 (1982)). Regarding counsel's responsibility to clients in a situation where the need for close corporation planning is indicated, see *supra* note 64 and *infra* text accompanying note 261.

¹²⁰ 591(C)(8). Discarding the board of directors would make sense in most single shareholder corporations.

¹²¹ 592(G). The transfer of liability to shareholders strongly suggests the appropriateness of the close corporation agreement addressing protection for any shareholder who will not participate in management. This might take the form of an indemnity from those who will be exercising the management function. Under the MODEL ACT SUPPLEMENT, if a corporation has eliminated the board of directors, a shareholder is not liable for any act or omission, although a director would be, unless the shareholder was entitled to vote on the action.

degree of displacement of the directors, in the form of restrictions on or delegation of their authority.¹²²

Another item of the laundry list aimed at achieving informality is the ability to avoid the requirement of having two persons sign documents,¹²³ by authorizing an individual holding more than one office to execute instruments in more than one capacity.¹²⁴ Thus, in the one shareholder corporation, the way has been cleared to eliminate, as in a sole proprietorship, the need for even the nominal involvement of any other individual in internal corporate affairs.¹²⁵ This would be achieved by discarding the board of directors and, in addition, designating the sole shareholder to fill all of the offices, with authority to execute any document in all his capacities. Such steps for the single shareholder corporation might well be taken by including in the articles of incorporation a short close corporation agreement effectuating these procedural simplifications.¹²⁶

The remaining laundry list items are concerned with the more significant substantive area of establishing the rights of individual shareholders vis-a-vis the corporation and other shareholders. In most cases these will be the building blocks for a wall of minority shareholder protection. Items concerned with protecting a shareholder's right to continuing income are the conferring of employment and compensation rights, with

MODEL ACT SUPPLEMENT § 21(C)(3). See *infra* text accompanying notes 169-71 recommending adoption of this approach as an amendment to 591.

¹²² 591(C)(8) permits delegation of the directors' authority to "other persons," as well as shareholders. This allows delegation to an outsider such as a management company, action that in the absence of 591 would be illegal. See H. HENN & J. ALEXANDER, *supra* note 11, at 575.

¹²³ The signatures of two prescribed officers are required by the OGCL for certificates filed with the Secretary of State with respect to an amendment to the articles of incorporation, a merger or consolidation, or a dissolution. O.R.C. §§ 1701.73, 1701.81, 1701.86.

¹²⁴ 591(c)(5). Cf. O.R.C. § 1701.64(a), which provides the opposite, but, of course, is subject to overriding action pursuant to 591. The Ohio Secretary of State has prescribed a form of "Close Corporation Affidavit," which "must accompany any certificate of amendment, dissolution, merger or consolidation that is signed by one person in two corporate capacities under § 1701.591 of the Ohio Revised Code."

¹²⁵ Practical considerations may, of course, dictate that another trusted person have the authority to execute documents on behalf of the corporation, in the event of the shareholder's unavailability.

¹²⁶ This is in contrast to the corporation where there are several shareholders and special arrangements relating to management, vetoes, compensation and other confidential matters are a part of the agreement. In that situation, in the interest of achieving confidentiality and ease of amendment, it would seem inadvisable to spread the close corporation agreement on the public records by including it in the articles of incorporation rather than in a private instrument. See 2 J. BLACKFORD, OHIO CORPORATION LAW AND PRACTICE § 15.181 (1985). For a form of a single shareholder close corporation agreement embodied in the articles of incorporation, see Appendix B.

no limitation as to duration,¹²⁷ and provisions governing distributions, dividends or division of profits.¹²⁸ Items concerned with protecting a shareholder's investment are: restricting the right of the corporation to sell either treasury stock or newly issued shares¹²⁹ and the power of one or more shareholders to cause the dissolution of the corporation.¹³⁰ Items directed to assuring rights to participate in management and major decisions are: permanent officer or director status;¹³¹ unanimous or other percentage voting requirements;¹³² the obligation to vote shares as specified;¹³³ and conferring on a shareholder the absolute right of access to corporate records and documents.¹³⁴

The final item of the laundry list authorizes arbitration as a means of breaking deadlocks among directors, as well as shareholders.¹³⁵

¹²⁷ 591(C)(6).

¹²⁸ 591(C)(7). This could include, for example, the mandatory payment of regular dividends or a distribution formula that differs from individual shareholdings. The possible effect of the latter type of provision on the corporation's Subchapter S tax status must be carefully considered. See *supra* note 111.

¹²⁹ 591(C)(10). Protection of this type could be expected ordinarily to go far beyond the pre-emptive rights conferred by O.R.C. § 1701.15, which are subject to a number of exceptions, including several that are quite broad. See *supra* note 46.

¹³⁰ 591(C)(2).

¹³¹ 591(C)(4).

¹³² 591(C)(3).

¹³³ *Id.* These few words are the only provision of the OGCL regarding voting (or "pooling") agreements among shareholders. In a voting agreement, the shareholders agree to vote their shares in a certain way on various matters or to pool their votes and cast them as a unit. H. HENN & J. ALEXANDER, *supra* note 11, at 535. Regarding the validity in Ohio of voting agreements that are not contained in a close corporation agreement, see *infra* note 156.

¹³⁴ 591(C)(9). This item eliminates the requirement of stating a "reasonable and proper purpose" under O.R.C. § 1701.37, which can be a difficult obstacle to overcome, often resulting in litigation. See *Lake v. Buckeye Steel Casting Co.*, 2 Ohio St. 2d 101, 206 N.E.2d 566 (1965). A shareholder's statutory right to inspection under O.R.C. § 1701.37 cannot be eliminated by a close corporation agreement. See *infra* note 150 and accompanying text.

¹³⁵ 591(C)(11). Arbitration, as a dispute resolution device, should be compared to appointment of a provisional director pursuant to O.R.C. § 1701.911. The latter section is intended to serve a somewhat similar purpose and is the most recent provision, prior to 591, added to the OGCL primarily for the benefit of close corporations. See OHIO GENERAL CORPORATION LAW 151 (Judson-Brooks ed. 1986) ("Committee Comment (1977)" to O.R.C. § 1701.911). In contrast to arbitration pursuant to a close corporation agreement, the right to the appointment of a provisional director is highly restricted by the statute. The right must be provided in the articles of incorporation or code of regulations. The appointment must be sought by a petition filed in the court of common pleas by not less than one-fourth of the directors or holders of one-fifth of the outstanding voting shares, and the petitioners must establish irreconcilable differences among the directors that have substantially impeded or made impossible the corporation's continued operations. The appointment is made by the court and the appointee serves until removed by the court or by holders of a majority of the voting shares. Access to the provisional director remedy, as for adoption of a close corporation agreement, requires elective action on the part of the corporation. Therefore,

Practically none of the management and control items of the laundry list could have been achieved prior to the enactment of 591 by the use of a single agreement among shareholders. Certain of the goals could likely have been accomplished by going "over under and through"¹³⁶ the OGCL by a combination of the devices of different classes of stock, an individual agreement between the corporation and each shareholder, and provisions in the articles of incorporation or code or regulations.¹³⁷ The simplification of corporate planning by permitting, instead, a single agreement allowing the parties to achieve their purpose directly and with certainty is sufficient justification for the enactment of 591. However, in addition, no matter how creative the documentation, prior to 591, the legality of granting lifetime officer status and employment rights was highly doubtful,¹³⁸ and there was clearly no lawful way to eliminate the board of directors¹³⁹ or to arbitrate deadlocks at the director level.¹⁴⁰

C. *Express Limitations on the Scope of a Close Corporation Agreement*

The permitted scope of a close corporation agreement is limited by specific reference in division (D) of 591 to certain other provisions of the OGCL.¹⁴¹ Division (D) invalidates any provision of a close corporation agreement that tampers with OGCL requirements governing the filing of

assuming shareholder unanimity is present, it is hard to conceive of a situation where it would not be preferable to adopt a close corporation agreement providing for arbitration as a dispute resolution device, rather than to go the provisional director route. The advantages of arbitration over a provisional director are obvious and great. Arbitration can be used to resolve any type of issue, not just director deadlocks. It is a simpler, more temporary, and less expensive remedy. It avoids court proceedings and a judicial appointment, possibly motivated by patronage or cronyism, as well as the intrusion of a stranger on the board of directors, whose presence may exacerbate rather than alleviate the underlying causes of shareholder friction.

¹³⁶ See Ginsberg, *supra* note 14, at 9.

¹³⁷ See MODEL ACT SUPPLEMENT at 1806 (Introductory Comment). The position taken there is that "by the use of sophisticated contracts among the shareholders and special provisions in the articles of incorporation and by-laws" any desired result achievable under the MODEL ACT SUPPLEMENT can be achieved under the REVISED MODEL BUSINESS CORPORATION ACT (1984), but that the SUPPLEMENT provides the advantages of certainty, flexibility, less drafting and lower probability that some factor has been overlooked. The same claim, however, cannot be made for the OGCL, which hardly compares to the sleek, modernized REVISED MODEL BUSINESS CORPORATION ACT. For example, the latter, in Section 8.01, goes so far as to duplicate Section 21 of the MODEL ACT SUPPLEMENT permitting elimination of the board of directors.

¹³⁸ See F. O'NEAL, *supra* note 10, at §§ 6.05, 6.06.

¹³⁹ See F. O'NEAL, *supra* note 10, at § 3.60.

¹⁴⁰ See H. HENN & J. ALEXANDER, *supra* note 11, at 748; 11 O. JUR. 3d *Business Relationships*, § 395, at 661 (1970).

¹⁴¹ The California close corporation law was the source of this provision. CAL. CORP. CODE § 300(c)(West 1986).

documents with the Secretary of State and their prescribed form,¹⁴² or with the provisions of eighteen specified sections of the OGCL.¹⁴³

Protection of the uniformity of the form of documents filed with the Secretary of State is self-explanatory. However, the reason for the list of "untouchable" sections in division (D)(2) is less obvious and consists of three distinct purposes. The first, which encompasses twelve of the eighteen sections,¹⁴⁴ reinforces, in a belt and suspenders approach, the limitation on the scope of a close corporation agreement to "internal affairs of the corporation or the relations of the shareholders among themselves."¹⁴⁵ Thus, this purpose is mainly concerned with assurances for creditors and other third parties dealing with the corporation.¹⁴⁶ The second purpose is far different. It represents a departure from 591's freedom of contract approach by preserving certain minimum rights of shareholders under the OGCL, which otherwise could be denied them by a close corporation agreement.¹⁴⁷ In this category are the rights to an annual financial statement,¹⁴⁸ the holding of an annual meeting,¹⁴⁹ and the inspection of corporate records for a reasonable and proper purpose.¹⁵⁰ The third purpose is concerned simply with protection against invalida-

¹⁴² 591(D)(1).

¹⁴³ 591(D)(2).

¹⁴⁴ O.R.C. §§ 1701.03, 1701.18, 1701.30, 1701.31, 1701.32, 1701.33, 1701.35, 1701.64, 1701.91, 1701.93, 1701.94 and 1701.95.

¹⁴⁵ 591(C).

¹⁴⁶ Included in these twelve sections are the traditional measures to preserve the integrity of the corporation's capital by limitations contained in O.R.C. §§ 1701.30 (requirement of stated capital), 1701.31 (reduction of stated capital) and 1701.32 (regulation of surplus), and by restricting the source of dividends and stock redemptions in O.R.C. §§ 1701.33 and 1701.35. A concession to the traditional corporate form for the purpose of facilitating dealing with third parties is the retention of the requirement that there be corporate officers as required by the first sentence of O.R.C. § 1701.64.

¹⁴⁷ A major purpose of 591 is to facilitate protection of minority shareholders by removing the barriers to a freely negotiated agreement between the majority and the minority factions. Yet, if certain mandatory shareholder protection provisions of the OGCL were not made off limits, the freedom of contract conferred on the parties by 591 could be used to increase the vulnerability of minority shareholders to oppression by the majority. The argument that the minority will have assented to same with full knowledge of the consequences may be of doubtful validity, depending on the minority's bargaining power, sophistication and other practical factors present at the time the corporate venture is organized. See *infra* note 194 and accompanying text.

¹⁴⁸ O.R.C. § 1701.38.

¹⁴⁹ O.R.C. § 1701.39. See *infra* text accompanying notes 172-76 for a recommended amendment to 591 to permit dispensing with the annual meeting, unless it has been formally requested by a shareholder.

¹⁵⁰ O.R.C. § 1701.37(C). In addition, divisions (A) and (B) of this section require the corporation to maintain books and records, and a list of shareholders. Cf. 591(C)(9), which permits the close corporation agreement to confer an absolute right on shareholders to access to the corporate records. See *supra* note 134.

tion of the close corporation agreement by an errant transfer of stock to an innocent purchaser.¹⁵¹

D. *Other Shareholder Agreements*

591 has revolutionized preexisting Ohio law relating to agreements among shareholders, but it has not displaced the preexisting law by providing the exclusive means of creating an agreement among shareholders.¹⁵² There is, however, no section of the OGCL relating to an agreement among shareholders that does not conform to the requirements of 591.¹⁵³ The single short sentence comprising division (L) eliminates any possible negative implication to be drawn from 591 concerning the validity of these nonconforming agreements. On the other hand, there would seem to be no reason why any agreement to which every shareholder of the corporation is a party, regardless of its content, should not be made a close corporation agreement under 591. Thus, there would be included in the single agreement every aspect of the shareholders' contractual agreements, whether partaking of the laundry list of division (C) or not.¹⁵⁴ That action would procure the protection of 591 for the agreement, and there could be no corresponding detriment in the event of the occurrence of an invalidating event under division (I),¹⁵⁵ since any possible taint of one provision on another would be removed by the division's savings clause.

E. *Savings Clause*

If the special protection of 591 is lost because of the occurrence of an invalidating event under division (I), the entire agreement, unless it otherwise provides, is not automatically nullified. Instead, under the savings clause contained in division (I), the validity of each individual

¹⁵¹ O.R.C. §§ 1701.24 and 1701.25 require that ownership of shares be evidenced by the issuance of stock certificates in the prescribed form. Division (F) of O.R.C. § 1701.24, permitting the existence of uncertificated shares, is made inoperative by 591(M), for any corporation that is the subject of a close corporation agreement. See *supra* text accompanying notes 105-09 (concerning the invalidation of a close corporation agreement resulting from the transfer of an unlegended stock certificate).

¹⁵² 591(L).

¹⁵³ A non-591 agreement among shareholders will often take the form of a "voting agreement." See *supra* note 133. Regarding the validity of voting agreements and possible legislation to clarify their validity, see *infra* note 156.

¹⁵⁴ The most common provisions not covered by the laundry list would be restrictions on the transfer of shares. For recommended legislation to recognize the validity of specific types of transfer restrictions, see *infra* text under heading "Need for additional Legislation-Share Transfer Restrictions."

¹⁵⁵ There are only two such events under 591(I), either the commencement of public trading in the stock or an unauthorized transfer of shares to a bona fide purchaser for value. See *supra* text accompanying notes 99 & 106.

provision of the agreement will be tested under other applicable Ohio law and, to the extent it is not invalid thereunder, will continue to be binding on the parties.¹⁵⁶

F. *Negation of Traditional Obstacles*

Few doctrines are more deeply rooted in American corporation law than the restrictive rules sought to be nullified by 591.¹⁵⁷ Therefore, prudence dictated that division (C)'s positive action in sanctioning the subject matter for inclusion in a close corporation agreement be bolstered by the additional assurance provided by division (F). The effect of division (F) is to immunize a freewheeling close corporation agreement from attack based on assertions that the agreement treats the corporation as if it were a partnership or the shareholders as if they were partners;¹⁵⁸ or that it provides for conducting the affairs of the corporation or relations among its shareholders in a manner that would be improper under the OGCL or other applicable law;¹⁵⁹ or that it interferes with the authority or discretion of the directors.¹⁶⁰

A similar provision with, however, a different purpose is found in division (K). There the failure, pursuant to a close corporation agreement, to observe corporate formalities relating to directors' or sharehold-

¹⁵⁶ Voting agreements among shareholders, which are not embodied in a valid close corporation agreement, are presumably legal in Ohio under the common law, if they do not have the effect of sterilizing the board of directors. Their status, however, is far from clear. See 12 O. JUR. 3d *Business Relationships*, § 576 (1970)(voting or pooling agreements). See also *supra* text accompanying notes 22-24. To be contrasted with the absence in the OGCL of any treatment of voting agreements (other than the brief mention in the 591(C)(3) laundry list) is the statutory recognition of voting trusts, which are authorized by O.R.C. § 1701.49, and are limited to a ten-year term, unless coupled with an interest. Most other states have laws enacted independently of special close corporation legislation, which generally recognize the rights of shareholders to enter into a written voting agreement. These statutes also declare the voting agreement's independence from statutory restrictions on voting trusts and provide for their enforcement by the remedy of specific performance. The annotation to MODEL BUSINESS ACT ANNOTATED § 7.31 (1984) lists thirty-six states that have statutes of this type (including an erroneous reference to Ohio). See, e.g., ILL. ANN. STAT. ch. 32 § 7.70 (Hurd-Smith Supp. 1985). Ohio might well give consideration to the adoption of such a statute to clarify the formalities required and enforcement remedies available for non-591 voting agreements. Of course, the enforceability of any particular provision of such an agreement would continue to be governed by provisions of the OGCL (other than 591) and by Ohio common law. See MODEL BUSINESS CORP. ACT ANNOT. § 7.31 (1984)(Official Comment). This would mean that, depending on the subject matter of the agreement, uncertainty as to validity could still be removed only by qualification as a close corporation agreement under 591. Nevertheless, in situations where less than all the shareholders are parties to the agreement, the adoption of such a statute would be a desirable improvement to the existing law.

¹⁵⁷ See *supra* text under heading "Overview of Close Corporation Legislation."

¹⁵⁸ 591(F)(1).

¹⁵⁹ 591(F)(2).

¹⁶⁰ 591(F)(3).

ers' meetings is eliminated as a factor in a court's determination of whether or not to pierce the corporate veil.¹⁶¹

G. Enforcement of Close Corporation Agreement

It is 591's intent that its policy favoring freedom of contract among shareholders not be frustrated by the refusal of a court to require a valid close corporation agreement to be performed pursuant to its terms. Accordingly, division (J) expressly authorizes a court of equity to enforce a close corporation agreement by injunction or specific performance. The division's purpose is to assure that a court will be sympathetic to the position of a person seeking specific enforcement, in the face of a claim that the requested relief is barred by availability of an adequate remedy at law.¹⁶²

VII. THE NEED FOR ADDITIONAL LEGISLATION

In this section, consideration will be given to possible further legislative action by the Ohio General Assembly to improve and complete the statutory plan for the Ohio close corporation. Attention will be directed to three topics; first to slight improvements in 591, next to validating stock transfer restrictions, and finally, to providing relief from shareholder oppression.¹⁶³

¹⁶¹ The close corporation statutes of a number of states include a provision of this type. See, e.g., CAL. CORP. CODE § 300(B) (West 1986). See also MODEL ACT SUPPLEMENT § 25. Rarely, however, have courts relied solely on informality in the conduct of a corporation's affairs as the basis for imposing personal liability on shareholders. See Downs, *Piercing the Corporate Veil Do Corporations Provide Limited Personal Liability?*, 53 UMKC L. REV. 174, 175 (1985); Karjala, *supra* note 64, at 1216. Comment, *Piercing the Corporate Veil in Maryland: An Analysis and Suggested Approach*, 14 BALTIMORE L. REV. 322 (1985). Adoption of a close corporation agreement should not, of course, have any effect on an attempt to pierce the corporate veil based on other grounds, such as undercapitalization.

¹⁶² See OHIO GENERAL CORPORATION LAW 93 (Judson-Brooks ed. 1986) ("Committee Comment (1981)" to 591).

¹⁶³ Mention is made above of the four components of a complete close corporation statutory scheme. See *supra* text accompanying notes 29-33. In enacting 591, Ohio has provided the means for the corporation to achieve informality in its internal operations and for the shareholders to reach agreement regarding management and control. Left unaddressed by 591, however, are transfer restrictions and shareholder oppression. The drafting of a close corporation law for the state of Ohio was a project commenced by the Close Corporation Subcommittee of the Corporation Law Committee of the Ohio State Bar Association in late 1977. See *Report of the Corporation Law Committee*, 53 OHIO ST. B. ASS'N REP. 510 (1980). The Subcommittee's original approach covered all four components. The part designed to sanction a list of stock transfer restrictions and the part providing self-executing relief in cases of shareholder oppression were dropped by the Corporation Law Committee in the late 1970's. In 1982, legislation providing a shareholder oppression remedy was again considered and rejected by the Committee. See *Minutes of Meetings of the Corporation Law Committee of the Ohio State Bar Association* (Sept. 9, 1978, Mar. 3, 1979,

A. *Improving 591*

Some Ohio lawyers have questioned the wisdom of permitting the close corporation agreement, in the absence of a contrary provision, to be amended or terminated by a four-fifths majority of all shares,¹⁶⁴ rather than by unanimous shareholder approval as required for the original authorization of the agreement.¹⁶⁵ The counterpart provisions of some other close corporation statutes opt for a requirement of shareholder unanimity for this purpose,¹⁶⁶ and commentators have voiced support for unanimity.¹⁶⁷ Four-fifths was originally selected by the drafters as a concession to the belief that there should be a presumption in favor of allowing the corporation's return to the corporate norm.¹⁶⁸ However, 591's more dominant policy of providing protection for minority shareholders argues for a reversal of the present statutory bias against an unwary shareholder owning no more than 20% of the stock. Accordingly, the statute should be amended to require unanimity for amendment or termination of a close corporation agreement, unless the agreement provides otherwise.

A provision of a close corporation agreement eliminating the board of directors can exclude one or more shareholders from participating in the substituted decision making process¹⁶⁹ and yet, at present, the statute provides that all of the shareholders succeed to the liability of the directors.¹⁷⁰ It would seem logical and fair, therefore, to add a provision absolving from liability under division (G)(2) of 591 any shareholder of a directorless corporation, who was not entitled to vote on the action giving rise to the exposure.¹⁷¹

With respect to most close corporations, the statutorily required annual meeting of shareholders is either ignored or is a meaningless exercise on paper. Thus, it is unrealistic, when a close corporation agreement is in effect, to preserve to its full extent the present inflexible requirement of holding an annual meeting.¹⁷² Therefore, as is provided by the laws of

Mar. 6, 1982). In view of subsequent developments and additional arguments advanced in this section of the article, it is the writer's belief that reconsideration, in greater depth, of the broadening of the scope of Ohio's close corporation legislation would be appropriate.

¹⁶⁴ 591(E).

¹⁶⁵ 591(A)(1).

¹⁶⁶ See, e.g., MODEL ACT SUPPLEMENT § 20(f); MD. CORPS. & ASS'NS CODE ANN. § 4-401(b)(1985); TEX. BUS. CORP. ACT ANN. art. 12.33B (Vernon 1980 & Supp. 1986).

¹⁶⁷ See, e.g., Kessler, *supra* note 39, at 666.

¹⁶⁸ There is precedent for the present approach. See, e.g., ILL. ANN. STAT. ch. 32 §§ 1205 and 1207. (Smith-Hurd 1970 Supp. 1985)(unanimity required for original election as close corporation and two-thirds for termination).

¹⁶⁹ 591(C)(8).

¹⁷⁰ 591(G).

¹⁷¹ Cf. MODEL ACT SUPPLEMENT § 21(c)(3); MD. CORPS. & ASS'NS CODE ANN. § 4-401(b)(1985).

¹⁷² An annual meeting is mandatory under O.R.C. § 1701.39, and that section appears as

other states,¹⁷³ the statute should permit a close corporation agreement to dispense with the annual meeting, unless a shareholder timely requests it.¹⁷⁴ In any event, the truly valuable right of shareholders under O.R.C. § 1701.38 to receive the corporation's annual financial statement¹⁷⁵ satisfies the essential purpose of an annual meeting in the case of most close corporations.¹⁷⁶

B. Share Transfer Restrictions

There is no requirement under 591 that shareholders agree to restrictions on the transfer of their shares in order that their agreement qualify as a close corporation agreement,¹⁷⁷ nor, on balance, does it appear that such a requirement would be advantageous.¹⁷⁸ However, in the vast majority of close corporations, such restrictions are highly desirable and will be an essential element of the overall plan adopted by shareholders.¹⁷⁹

an "untouchable" in division (D)(2) of 591. As is true with respect to a number of provisions of the OGCL, a close corporation agreement will likely supplant action that might otherwise be taken by a vote of shareholders at an annual meeting.

¹⁷³ See, e.g., MD. CORPS. & ASS'NS CODE ANN. § 4-402 (1985); MODEL ACT SUPPLEMENT § 23(b).

¹⁷⁴ The preferable way to accomplish this change would be by retaining O.R.C. § 1701.39 as an "untouchable" in division (D)(2) of 591 and, instead, amending O.R.C. § 1701.39 to permit this relaxation of the annual meeting requirement, if contained in a close corporation agreement.

¹⁷⁵ This right is preserved as an "untouchable" under 591(D)(2).

¹⁷⁶ If the mandatory annual meeting requirement were relaxed, a conforming amendment to O.R.C. § 1701.38 would be necessary to assure continuation of the right to an annual statement. This follows from the present requirement in O.R.C. § 1701.38 of the presentation of the annual statement at the annual meeting and the mailing of the copy to a shareholder requesting it within sixty days after notice of the meeting has been given.

¹⁷⁷ 591(A). Even though the "laundry list" of 591(C) makes no reference to share transfer restrictions, the subject is clearly appropriate for optional inclusion in a close corporation agreement, as being within the broad grant of authority in the opening paragraph of 591(C). See *supra* note 154.

¹⁷⁸ The close corporation statutes of some other states do impose such a requirement. See, e.g., DEL. CODE ANN. tit. 8 § 342 (a)(2)(1983); PA. STAT. ANN. tit. § 1372.A(2)(Purdon Supp. 1985). The MODEL ACT SUPPLEMENT prescribes a standardized transfer prohibition that automatically applies unless the articles of incorporation provide otherwise. MODEL ACT SUPPLEMENT §§ 11 & 12. The drafters of 591, however, came to the conclusion that the use of a close corporation agreement should not be denied to shareholders who, for their own reasons, have decided not to impose transfer restrictions. See Karjala, *supra* note 64, at 1257. Moreover, the close corporation agreement itself, as publicized by the required legend on the stock certificates, will serve to inhibit transfers.

¹⁷⁹ As in the case of partners, close corporation shareholders most often desire to make sure that the principle of *delectus personae* is applicable to their relationship. See Kessler, *supra* note 39, at 665. The possible loss of the corporation's Subchapter S status under the Internal Revenue Code by reason of the transfer of a stockholder's shares has, in recent times, given added incentive to the adoption of transfer restrictions. See F. O'NEAL, *supra*

Since stock transfer restrictions are a form of restraint against the alienation of property, in the absence of authorizing legislation or judicial sanction, their enforceability is uncertain.¹⁸⁰ Absolute prohibitions on transfer, unlimited in time, have traditionally been held to be unreasonable restraints and, therefore, invalid.¹⁸¹ In addition, restrictions requiring the consent of the corporation or of the director or other shareholders to the transfer of shares are of questionable validity.¹⁸² However, restrictions conferring a right of first refusal on the part of the corporation or the other shareholders are generally upheld.¹⁸³

The OGCL is silent on the subject of the validity of transfer restrictions,¹⁸⁴ and the Ohio decisions, although inconclusive, appear to follow the established general rules.¹⁸⁵

It would, therefore, be beneficial to clarify and facilitate this important aspect of close corporation planning by the adoption of legislation broadly recognizing the validity of the most common type transfer restrictions, including the right of the corporation or shareholders to block a transfer by withholding consent.¹⁸⁶ The addition for this purpose of a new section to the OGCL applicable to all corporations¹⁸⁷ should be welcomed as strengthening, independently of 591, the resources available to Ohio close corporation planners.

note 10, at § 7.02. For reference to a different, although related, aspect of Subchapter S status, see *supra* note 111.

¹⁸⁰ See 2 J. BLACKFORD, *supra* note 126, at § 51.10; Note, *supra* note 14, at 627, 628.

¹⁸¹ F. O'NEAL, *supra* note 10, at § 7.06.

¹⁸² F. O'NEAL, *supra* note 10, at § 7.08; Rands, *Closely Held Corporations: Restrictions on Stock Transfers*, 84 COM. L. J. 461, 464 (1979).

¹⁸³ F. O'NEAL, *supra* note 10, at § 7.09. Rands, *supra* note 181, at 463.

¹⁸⁴ O.R.C. § 1701.11(B)(8) merely authorizes inclusion in a corporation's code of regulations of "restrictions on the right to transfer [shares]."

¹⁸⁵ See 62 O. JUR. 3d *Investment Securities*, §§ 30, 33 (1985); Barron, *Arrangements Validity and Enforcement of Restrictions on Share Transfer and Buy-Out. Various Types of Restrictions in Ohio*, 31 U. CIN. L. REV. 266, 267-69 (1962).

¹⁸⁶ As in the case of a partnership, the property law concept disfavoring restraints on alienation should give way to the principles of *delectus personae* and freedom of contract among the participants in the venture. See Johnson, *supra* note 79, at 798-99.

¹⁸⁷ This would seem to be the better of two possible approaches and is the one adopted by a number of states. F. O'NEAL, *supra* note 10, at § 7.06A. The alternative, a more limited approach, would be to add another item to the "laundry list" in division (C) of 591 referring generally to restrictions on share transfers, including the specific sanctioning of a "consent" requirement. The objective would be, in keeping with the purpose of the laundry list, to remove all doubt as to the validity of an otherwise invalid consent restriction in a close corporation agreement. Presumably, this would overcome the common law impediment to transfer restrictions based on principles of property law. It should not be overlooked that the position can be taken that 591, in its present form, authorizes transfer restrictions otherwise invalid under Ohio common law. Reliance for this proposition would be on the opening paragraph of division (C), which broadly defines the permitted scope of a close corporation agreement. See *supra* text accompanying notes 113-15.

C. Relief from Shareholder Oppression¹⁸⁸

It is not a purpose of this article to cover this complex subject in great depth.¹⁸⁹ However, substantial treatment is necessary, at the risk of otherwise presenting a seriously incomplete assessment of the current status under Ohio law of the close corporation and its shareholders, especially minority shareholders.¹⁹⁰

The traditional corporate structure and norms, especially the principle of majority control and the business judgment rule, make it easy for those in control of the corporation to take advantage of minority shareholders.¹⁹¹ In addition, the illiquidity of the latter's investment seals off any means of escape.¹⁹²

A major premise supporting the enactment of 591 is that the best protection for shareholders in a close corporation is that for which they have bargained as a result of engaging in advance planning with their fellow shareholders.¹⁹³ Ideally, the prospective business associates, guided by competent and knowledgeable counsel, will work out an agreement pursuant to 591 covering all pertinent reciprocal rights and obligations. In the real world, it may only occasionally happen that way. It must be recognized that, for any number of reasons, in most cases the shareholder relationship will not be adequately provided for at the inception of the venture.¹⁹⁴ As a result, situations will often arise later where one faction will seek to exercise its power unfairly to the disadvantage of the other. Practically all such cases will involve oppression by the majority directed against the minority, but the opposite is possible as

¹⁸⁸ The more descriptive terms "squeeze-out" and "partial squeeze-out" are employed by Professors O'Neal and Thompson throughout their treatise to refer to the oppressive tactics directed by controlling shareholders against minority shareholders. F. O' NEAL & R. THOMPSON, *supra* note 19.

¹⁸⁹ Full treatment of the topic would require another article of equal or greater length. Such an effort is unnecessary, however, due to the existing wealth of literature in the area, consisting of the two-volume treatise by Professors O'Neal and Thompson, and numerous articles including, most recently, Olson, *A Statutory Elixir for the Oppression Malady*, 36 MERCER L. REV. 627 (1985).

¹⁹⁰ See *infra* note 263.

¹⁹¹ F. O'NEAL & R. THOMPSON, *supra* note 19, at § 3.03. See also Olson, *supra* note 189, at 627-28; Peeples, *The Use and Misuse of the Business Judgment Rule in the Close Corporation*, 60 NOTRE DAME L. REV. 456, 487 (1985); *supra* text accompanying notes 18-21.

¹⁹² See F. O'NEAL & R. THOMPSON, *supra* note 19, at § 2:15; Hetherington & Dooley, *supra* note 81, at 6; Kessler, *supra* note 39, at 689. But see Easterbrook and Fischel, *supra* note 24, at 274-77.

¹⁹³ See *supra* text under headings "Introduction" and "Objective, Philosophy and Approach of 591."

¹⁹⁴ See Hetherington and Dooley, *supra* note 81, at 36, 37; Olson, *supra* note 189, at 633; Peeples, *supra* note 191, at 490, 491.

a result of the oppressive exercise of contractual veto rights possessed by the minority.¹⁹⁵

Two recent Ohio cases involve typical fact patterns illustrating the unfair treatment of a minority shareholder by the majority. In *Estate of Schroer v. Stamco Supply Inc.*,¹⁹⁶ the controlling shareholders caused the corporation to repurchase the shares held by some members of their group, while denying the same opportunity to the plaintiff minority shareholder. In *Soulas v. Troy Donut Univ., Inc.*,¹⁹⁷ two of the three equal shareholders voted to increase their salaries to the point where the profit of their subchapter S corporation,¹⁹⁸ previously distributed equally among the three, was eliminated.¹⁹⁹

The policy of providing strong judicial relief to close corporation shareholders from oppressive action taken by the controlling faction can no longer be disputed. The principle has been endorsed by the laws of a number of states,²⁰⁰ judicial decisions,²⁰¹ and virtual commentator unanimity.²⁰² These authorities have rejected the application of the traditional corporate norms discussed above²⁰³ as the standard by which to measure the conduct of the controlling interest toward minority shareholders. Instead, new standards have been formulated by them, in terms of the majority's partnershiplike "fiduciary duty" to minority shareholders,²⁰⁴ and its obligation not to act "oppressively or unfairly"²⁰⁵ or in a

¹⁹⁵ See Olson, *supra* note 189, at 638 n. 71. Oppressive conduct by the minority against the majority is obviously a rare occurrence, and is likely to involve closer policy questions since it is the allegedly wrongful exercise of a bargained-for right given presumably to insure the minority's protection. Closer questions are also present where the minority is asserting the misconduct of the majority in spite of the existence of a close corporation agreement. In both situations it would seem that the plaintiff should be held to a heavier burden to establish a right to relief. The balance of the discussion in this section will be in the context of majority oppression of the minority, but much of it would be pertinent if the opposite fact pattern was present. See MODEL ACT SUPPLEMENT § 40, at 1852 (Official Comment).

¹⁹⁶ *Estate of Schroer v. Stamco Supply, Inc.*, 19 Ohio App. 3d 34, 482 N.E.2d 975 (1984).

¹⁹⁷ *Soulas v. Troy Donut Univ. Inc.*, 9 Ohio App. 3d 339, 460 N.E.2d 310 (1983).

¹⁹⁸ See *supra* notes 111 and 179 (concerning issues relating to corporations that have elected Subchapter S status under the Internal Revenue Code).

¹⁹⁹ The two cases are analyzed, *infra* in the text accompanying notes 212-221.

²⁰⁰ See, e.g., MICH. COMP. LAWS ANN. § 450.1825(a)(West 1973 & Supp. 1980); MINN. STAT. ANN. § 302A.751, Subd. 1(b)(2)(West 1980); N.J. REV. STAT. ANN. § 14A:12-7(1)(c)(West 1969 & Supp. 1985); N.D. CENT. CODE § 10-19.1-115 (1985). See also MODEL ACT SUPPLEMENT § 40.

²⁰¹ For a list of cases decided in the past sixteen years, see Olson, *supra* note 189, at 649.

²⁰² For a list of articles, see Olson, *supra* note 189, at 629 n.14. But see Easterbrook & Fischel, *supra* note 24, at 283-301.

²⁰³ See *supra* text accompanying notes 19-21 and 191.

²⁰⁴ See *Estate of Schroer v. Stamco Supply, Inc.*, 19 Ohio App. 3d 34, 40, 482 N.E.2d 975 (1984); *Donahue v. Rodd Electrottype Co.*, 367 Mass. 578, 328 N.E.2d 505 (1975); see *infra* text accompanying notes 215-18.

²⁰⁵ N.J. REV. STAT. ANN. § 14A 12-7(1)(c)(West 1969 & Supp. 1985).

"manner unfairly prejudicial"²⁰⁶ toward the minority or in disregard of the minority's "reasonable expectations."²⁰⁷ This modern approach shares a common rationale with preventive legislation such as 591, in the recognition that the relationship of shareholders of a close corporation should be governed by essentially the same principles as are applicable to partners.²⁰⁸

In spite of the well-established trend toward providing relief from shareholder oppression, until recently there has been no progress in Ohio on either the legislative or the judicial front. Ohio's laggard status is most strikingly evidenced by its legislative inaction. Most other states have provided a statutory remedy for at least the most severe oppressive tactics against a shareholder, by making such wrongdoing a ground for judicial dissolution.²⁰⁹ In addition, a number of states have enacted laws making available to courts a variety of innovative and flexible remedies to combat shareholder oppression.²¹⁰ However, in sharp contrast, the OGCL, including its section on judicial dissolution,²¹¹ has remained completely silent on the subject of shareholder oppression. There simply is no statutory recognition in Ohio of the possible existence of such a wrong, no matter how aggravated, for which a court might grant a remedy.

On the judicial front, however, the silence recently ended with the handing down of the above mentioned *Schroer*²¹² and *Soulas*²¹³ decisions at the appellate court level. In both of these cases, relief was granted to a minority shareholder as a result of overreaching conduct on the part of

²⁰⁶ MINN. STAT. ANN. § 302A.751, Subd.1(b)(2)(West 1985). See also MODEL ACT SUPPLEMENT § 40(a)(1).

²⁰⁷ MINN. STAT. ANN. § 302A.751, Subd.3a(West 1985).

²⁰⁸ See *supra* note 204.

²⁰⁹ See Hetherington & Dooley, *supra* note 81, at 17 n.45. The shareholder oppression legislation of other states is discussed *infra*, in notes 235-45 and accompanying text.

²¹⁰ See, e.g., MICH. COMP. LAWS ANN. § 450.1825 (West 1973 & Supp. 1980); S. C. CODE ANN. § 33-21-155 (Law. Co-op. Supp. 1984); WIS. STAT. ANN. § 180.995(19)(West Supp. 1985)(patterned after MODEL ACT SUPPLEMENT §§ 41 & 42. See also *supra* notes 205-07.

²¹¹ O.R.C. § 1701.91. This section's only ground for dissolution relating to conflict among shareholders is a deadlock on the part of directors in the management of corporate affairs, or on the part of shareholders in the election of directors. O.R.C. § 1701.91(A)(4). A casual reading of division (A)(3) of the section might suggest the possibility of a dissolution suit based on shareholder oppression. The ground there stated is that dissolution would be "beneficial to the shareholders." In the absence of a special provision in the articles, however, the action may be brought only by shareholders owning a majority of voting shares. Furthermore, this provision keys on protection of shareholders as a whole and is, therefore, inapplicable to instances of majority oppression of the minority. See Hetherington & Dooley, *supra* note 81, at 9-19.

²¹² See *supra* text accompanying note 196.

²¹³ See *supra* text accompanying note 197.

the majority, notwithstanding that the corporation's improper action had been taken by authority of the board of directors.²¹⁴

In a strong opinion, the court in *Schroer* addressed what it found to be questions of first impression in Ohio.²¹⁵ The court affirmed the trial court's order requiring the corporation to purchase the minority shareholder's stock on the same basis as its earlier purchase of shares from a member of the controlling shareholder group. In so doing, it held that the controlling group owed an obligation to minority shareholders "substantially akin to that fiduciary duty owed by one partner to another to deal inter se in the utmost good faith."²¹⁶ The court followed the leading case of *Donahue v. Rodd Electrottype Co.*²¹⁷ and quoted language from that opinion establishing in unequivocal terms the existence of the partner-like fiduciary duty among stockholders in a close corporation.²¹⁸ The decision was not appealed to the Ohio Supreme Court.

The court in *Soulas* required the two majority shareholders to refund excessive salaries paid to them by the corporation to the detriment of the minority shareholder. The decision was based on a section of the OGCL authorizing directors by majority vote to establish "reasonable" compensation for services performed by directors and officers.²¹⁹ In addition to finding that the compensation was unreasonable, the court did, in dictum, recognize a cause of action by minority shareholders against controlling shareholders for diversion of corporate profits at the expense of the minority.²²⁰ However, the opinion nowhere else refers to any duty of the majority to the minority, despite the strong assertion of the same in the minority shareholder's brief.²²¹

²¹⁴ The court in *Soulas* apparently attached no significance to the fact that the aggrieved minority director received no notice of the meeting of directors at which the two majority directors, acting alone, increased their salaries. 9 Ohio App. 3d at 340-41, 460 N.E.2d at 312.

²¹⁵ 19 Ohio App. 3d at 34, 482 N.E.2d at 976.

²¹⁶ 19 Ohio App. 3d at 40, 482 N.E.2d at 981.

²¹⁷ *Donahue v. Rodd Electrottype Co.*, 367 Mass. 578, 328 N.E.2d 505 (1975).

²¹⁸ 19 Ohio App. 3d at 39, 482 N.E.2d at 981. The court also cited favorably another of the early leading cases, *Jones v. H. F. Ahmanson & Co.*, 1 Cal.3d 93, 360 P.2d 464, 81 Cal. Rptr. 592 (1969), and the more recent decision in *Alaska Plastics Co. v. Coppock*, 621 P.2d 270 (Ala. 1980). In addition, it quoted with favor from the earlier edition of O'NEAL'S OPPRESSION OF MINORITY SHAREHOLDERS.

²¹⁹ O.R.C. § 1701.60(A)(3). See *Soulas*, 9 Ohio App.3d at 341, 460 N.E.2d at 312-13.

²²⁰ *Soulas*, 9 Ohio App.3d at 342, 460 N.E.2d at 313.

²²¹ Plaintiff-Appellant Brief, at 17, 18, *Soulas*. In support of their assertion, counsel cited 12 O. JUR. 3d *Business Relationships*, § 528 (1979), which does indeed talk in terms of the fiduciary nature of the duty of the majority or dominant group to deal fairly with the corporation and its other shareholders. However, the concept of fiduciary duty so referred to is the universally recognized standard of conduct applicable to all corporations, publicly traded as well as close. It imposes a far less stringent obligation on the controlling shareholders and should not be confused with the higher partnership-like standard of fiduciary responsibility applied to the controlling shareholders of a close corporation. See H.

Given the solid base of support for the policy of protecting the rights of oppressed minority shareholders, the question boils down to selection of the proper approach to develop such protection. Should Ohio take statutory action to provide a remedy for implementation by the courts or, instead, should the task be left solely to the further development of relief by judicial decision?

It might be argued, especially in view of the two recent Ohio appellate decisions, that the more conservative position of allowing the remedy to develop through judge-made law is warranted. Such a hands-off approach, however, would be shortsighted and faulty for several compelling reasons.

First, the effect of the cases must be realistically viewed. Two Court of Appeals decisions "do not make a summer."²²² Their fact patterns present garden variety types of shareholder oppression, while the ingenuity of controlling shareholders over the years has spawned an amazing array of different techniques to accomplish their improper objectives.²²³ In order to combat effectively modern-day shareholder oppression, what is needed is the flexibility that only legislation can provide, by broadly defining the wrongdoing condemned and by supplying an opposing arsenal of varied and innovative types of relief.²²⁴ Shareholder oppression is too deep-

HENN. & J. ALEXANDER, *supra* note 11, at §§ 240 & 268. It appears that prior to the *Schroer* decision there was no judicial recognition in Ohio of a partnershiplike fiduciary duty applicable to close corporations. The *Schroer* opinion, however, equivocally states that "[i]n Ohio, the [fiduciary relationship] principle has received somewhat less explicit, although a nevertheless inferable, expression in the area of the authority of corporate directors or majority shareholders to redeem or retire corporate stock" citing a 1910 Ohio Court of Common Pleas decision and finding that "[t]he federal courts applying what they found to be the Ohio law, assume the existence of a fiduciary duty between shareholders of a close corporation. . . ." *Schroer*, 19 Ohio App. 3d 34 at 39, 482 N.E.2d at 980. The opinion relies on 591 to support its conclusion that partnership principles are properly applicable to the close corporation: "[B]y this enactment [of 591] Ohio has signalled its recognition of the eclectic tendencies of the close corporation in blending features of the corporate and the partnership form. . . ." 19 Ohio App. 3d at 37, 482 N.E.2d at 979.

²²² A fair evaluation of the two cases would indicate that *Schroer* is an important decision and directly in the mainstream of contemporary developing protection for the rights of minority shareholders of close corporations. *Soulas*, however, was narrowly decided and no reliance was placed on principles of law peculiar to close corporations; it is therefore of far less value as a precedent in the general area of shareholder oppression.

²²³ Professors O'Neal and Thompson devote most of four chapters, consisting of 562 pages, to "squeeze-out" techniques. See F. O'NEAL & R. THOMPSON *supra* note 19 (chapters 3-6). See also Wells, *Involuntary Dissolution as a Remedy for Freeze-outs of Minority Shareholders: Two West Virginia Statutes*, 88 W. VA. L. REV. 47, 51 (1985).

²²⁴ Courts have generally been reluctant to grant nonstandard remedies in the absence of authorizing legislation. O'Neal, *supra* note 25, at 874; MODEL ACT SUPPLEMENT § 41 (Official Comment). See also *Apicella v. Pat Corp.*, 17 Ohio App. 3d 245, 249, 479 N.E.2d 315 (1984)(court can order directors to set a fair rental fee, but cannot itself determine the amount).

seated²²⁵ and complex a problem to deal with by the slow and uneven case-by-case development of law by Ohio courts.²²⁶

In addition, enactment of an oppression relief law would result in a balanced legislative treatment of the special needs of the shareholders of Ohio close corporations. It would add to the preventive law planning option made available by 591 a remedial response to the needs of oppressed shareholders who have failed to bargain for protection. Improving the weak position of the minority and, conversely, curbing the nearly absolute power of the majority, should encourage the parties' use of a close corporation agreement, by giving the majority incentive to bargain with the minority at the inception of the relationship.²²⁷ The resulting application of the carrot and stick principle should raise the level of close corporation shareholder harmony. In cases where the opportunity to bargain has not been utilized, a statutory oppression remedy would deter oppressive conduct by the majority²²⁸ and would encourage out-of-court settlement of shareholder disputes.²²⁹

Finally, the surprising absence in Ohio, in this modern day and in unfavorable contrast to most other states, of *any* statutory recognition of the problem of shareholder oppression must be confronted.²³⁰ This untenable situation requires, in order to clear the air, that there be, by the adoption of special legislation, an unequivocal expression of the public policy of the state of Ohio favoring oppression relief.²³¹ The

²²⁵ See F. O'NEAL & R. THOMPSON, *supra* note 19, at § 1:04.

²²⁶ See D. WETZEL, *LEGISLATIVE LAW AND PROCESS: CASES AND MATERIALS* 3, 7 (1986).

²²⁷ See Peeples, *supra* note 191, at 504. At the present time, a knowledgeable minority shareholder has great incentive to seek a close corporation agreement, and the majority shareholder has little incentive. Unfortunately, however, it is the majority that is typically in the position to implement 591, because of its influential role and closer relationship with the attorney handling the organization of the venture.

²²⁸ See F. O'NEAL & R. THOMPSON, *supra* note 19, at § 10:09.

²²⁹ Counsel for the minority shareholder has advised that, following the denial of certification by the Ohio Supreme Court, the *Soulas* case was settled by the majority shareholders' purchase of all the minority's shares. This type of settlement, assuming that the minority receives a price approaching fair value, would seem to be the best result in many of these cases. See, e.g., *Balvik v. Sylvester*, 2 Corp. Counsel weekly (BNA) No. 35, P.1 (Aug. 20, 1987). Professors Hetherington and Dooley have urged that it is the *only* feasible solution. See *infra* note 246 and accompanying text. A buy-out ordered by the court is a prominent option in the list of various remedies contained in modern shareholder oppression statutes. See, e.g., MODEL ACT SUPPLEMENT § 42; MICH. COMP. LAWS § 450.1825 (1973); MINN. STAT. ANN. § 302A.751 Subd. 2 (West 1985); N.J. REV. STAT. § 14A:12-7 (West 1969 & Supp. 1985); N.Y. BUS. CORP. LAW § 1118 (McKinney 1986); S.C. CODE ANN. § 33-21-150 (Law. Co-op. 1977). See also N.Y. BUS. CORP. LAW § 1118 (McKinney 1986) (conferring an option on the remaining shareholders to buy out a shareholder who has petitioned for involuntary dissolution pursuant to N.Y.B.C.L. § 1104-a on grounds of improper conduct on the part of the controlling persons).

²³⁰ See *supra* note 211 and accompanying text.

²³¹ See Olson, *supra* note 189, at 659.

practical side of the coin, with which there can surely be no disagreement, is the clear need to overhaul Ohio's outdated and ineffectual involuntary dissolution statute.²³² If that section of the OGCL is to be replaced, as it certainly must,²³³ it would seem appropriate to adopt a new law that will accord with present-day thinking on the subject of dealing with serious ruptures of the close corporation shareholder relationship.²³⁴

The balance of this section will consider the form that an Ohio shareholder oppression statute might take. The statutes of other states and the Model Act Supplement exhibit a variety of approaches to this type of legislation. The Model Act Supplement includes the oppression remedy as a separate section applicable to a corporation electing close corporation status.²³⁵ By the same token, it thereby excludes from the section's coverage all close corporations that have not made the election.²³⁶ Other states have enacted self-executing provisions²³⁷ affording automatic protection to the shareholders of all corporations within the category designated by the statute.

In defining the corporation whose controlling shareholders' conduct will be subject to scrutiny, existing legislation runs the gamut.²³⁸ The relief provided under some state laws is available only to corporations having no more than a prescribed maximum number of shareholders.²³⁹ Relief is made available by New York to shareholders of all nonpublicly

²³² O.R.C. § 1701.91. See Haynsworth, *The Effectiveness of Involuntary Dissolution Suits as a Remedy for Close Corporation Dissension*, 35 CLEV. ST. L. REV. 25, 84 (1986) ([I]n states like Ohio . . . involuntary dissolution by minority shareholders is virtually impossible because of overly restrictive statutes . . .).

²³³ The statute should, at the least, include "oppression" as a ground for involuntary dissolution, as in the REVISED MODEL BUSINESS CORPORATION ACT § 14.30 (1984). (See *infra* note 243.) This might give a court a peg on which to hang its hat in fashioning some other type of relief where, as is more often the case, the facts do not justify the severe remedy of dissolution. See, e.g., *Balvik v. Sylvester*, 2 Corp. Counsel weekly (BNA) No. 35, P. 1 (Aug. 20, 1987); *Masinter v. Webco Co.*, 262 S.E.2d 433 (W. Va. Sup. Ct. App. 1980) (discussed in Wells, *supra* note 223, at 66-67).

²³⁴ In addition to modern legislation in effect in other states, this recommendation is strongly supported by the trend of the American common law of corporations. Olson, *supra* note 189, at 634.

²³⁵ MODEL ACT SUPPLEMENT § 40. See also WIS. STAT. ANN. § 180.995(19) (West 1986).

²³⁶ The election must be made by a statement contained in the articles of incorporation. MODEL ACT SUPPLEMENT § 3.

²³⁷ See, e.g., MICH. COMP. LAWS § 450.1825 (1973); MINN. STAT. ANN. § 302A.751 (West 1985); N.J. REV. STAT. § 14A:12-7 (West 1969 & Supp. 1985); N.D. CENT. CODE § 10-19.1-115 (1985); S. C. CODE ANN. § 33-21-150 (Law. Co-op. 1977).

²³⁸ Only self-executing laws are referred to in this paragraph.

²³⁹ See, e.g., CAL. CORP. CODE § 800(b)(5) (West Supp. 1980) (35 shareholders); MINN. STAT. ANN. § 302A.751, 302A.011 Subd. 6a (West 1985) (35 shareholders); N.J. REV. STAT. § 14A:12-7(1)(a) (West 1969 & Supp. 1985) (25 shareholders); N.D. CENT. CODE § 10-19.1-115 (1985) (35 shareholders).

traded corporations,²⁴⁰ and by the remaining states, theoretically, to all corporations, whether close or publicly traded.²⁴¹

Most of the older statutes limit relief to the drastic, disfavored, and generally unsatisfactory remedy of judicial dissolution,²⁴² when it can be established that "the directors or those in control of the corporation have acted, are acting or will act in a manner that is illegal, oppressive, or fraudulent."²⁴³ The newer statutes,²⁴⁴ however, provide an array of broad equitable relief, which may be invoked by the court in its discretion as an alternative to dissolution. These laws have also dramatically lowered the threshold of remediable wrongdoing to include conduct that is "substantially prejudicial" to the petitioners.²⁴⁵ The ultimate relief for minority shareholders is that proposed by Professors Hetherington and Dooley. They advocate legislation conferring on the minority the unfettered right at any time of their choos-

²⁴⁰ The New York law empowers only holders of 20% or more of all outstanding shares to petition for relief. N.Y. BUS. CORP. LAW § 1104-a (McKinney 1986). The laws of all other states mentioned confer standing on any individual shareholder to seek relief.

²⁴¹ In this category fall only a few statutes of the modern type found in the states listed in *supra* notes 200 and 237. See MICH. COMP. LAWS § 450.1825 (1973); N.C. GEN. STAT. §§ 55-125(4), 55-125.1 (1982); S. C. CODE ANN. §§ 33-21-150(4), 33-21-155 (Law. Co-op. 1977). The large remaining balance of these statutes are the older typical involuntary dissolution laws modelled on MODEL BUSINESS CORP. ACT § 97 (1969). See *infra* note 243.

²⁴² MODEL ACT SUPPLEMENT § 40 at 1852 (Official Comment); O'Neal, *supra* note 25, at 882.

²⁴³ MODEL BUSINESS CORP. ACT § 97 (1969), which has been carried over as REVISED MODEL BUSINESS CORP. ACT § 14.30(a)(1984). Section 97 has been adopted by a number of states as their involuntary dissolution statute. See, e.g., N. H. REV. STAT. ANN. § 293-A:98(1977); OR. REV. STAT. § 57.595 (1985); VA. CODE ANN. § 13.1-747 (1985). Consequently, the quoted language defines the actionable wrong in the oppression relief provision of the corporation law of most of the states that deal with the problem legislatively. Compared to modern standards, it is a restrictive test that is generally met only by a showing of severe misconduct by the controlling shareholders. See Olson, *supra* note 189, at 639.

²⁴⁴ See *supra* notes 200 and 237.

²⁴⁵ See MINN. STAT. ANN. § 302A.751 Subd. 1(b)(2)(West 1985); N.D. CENT. CODE § 10-19.1-115-1(b)(2)(1985); WIS. STAT. ANN. § 33-21-150(a)(4)(West Supp. 1985); MODEL ACT SUPPLEMENT § 40(a)(1). The Minnesota and North Dakota laws further provide that:

[I]n determining whether to order equitable relief, dissolution, or buy-out, the court shall take into consideration the duty which all shareholders in a closely-held corporation owe one another to act in an honest, fair, and reasonable manner in the operation of the corporation and the reasonable expectations of the shareholders as they exist at the inception and develop during the course of the shareholders' relationship with the corporation and with each other.

MINN. STAT. ANN. § 302(A).751, Subd. 3a (West 1985); N. D. CENT. CODE § 10-19.1-115-3 (1985).

The "reasonable expectations" standard has been the linchpin of Professor O'Neal's campaign for shareholder oppression statutory relief for the last 30 years. O'Neal, *supra* note 25, at 885-88.

ing to require the corporation to purchase their stock at its fair value.²⁴⁶ No state, however, has yet adopted this provocative concept.²⁴⁷

In drafting shareholder oppression legislation for Ohio, advantage should be taken of the examples provided by the laws of other states and the Model Act Supplement,²⁴⁸ as well as the rich supply of the analyses and proposals of legal scholars.²⁴⁹ Drawing upon these sources, the author's recommendations as to the principal features of an Ohio statute are briefly stated below.

Because the legislation is remedial, its advantages should be available to all parties who are within the group intended to be protected, without any technical barriers. Therefore, no prior election of close corporation status, whether by means of a close corporation agreement or otherwise, should be a prerequisite to eligibility for relief. Certainly, shareholders who have not, through use of a close corporation agreement, engaged in planning to avoid the events giving rise to future oppression have the greatest need for the protection.²⁵⁰ Thus, the law should be self-executing

²⁴⁶ Hetherington & Dooley, *supra* note 81. The proposal has been strongly criticized. See Easterbrook & Fischel, *supra* note 24, at 288-90 (asserting a number of reasons why the unconditional right to withdraw capital is undesirable); Kessler, *supra* note 39, at 690 (asserting the "enormous potential it offers for oppression by a minority").

²⁴⁷ See Peeples, *supra* note 191, at 490. The Hetherington and Dooley proposal has the considerable advantage of being the most simple solution to the problem, and it may not be so radical as first appears when its partnership law antecedents are recognized. Under the UNIFORM PARTNERSHIP ACT any partner has the power to cause dissolution even if such action is in contravention of the partnership agreement. In such event, the dissatisfied partner is liable for damages and the remaining partners may continue the business if they purchase his interest. See A. BROMBERG & J. CRANE, CRANE AND BROMBERG ON PARTNERSHIP § 75 at 428 (1968); UNIFORM PARTNERSHIP ACT §§ 31(2), 38(2) (1910). Professors Hetherington and Dooley, however, are proposing a more liberal remedy for the minority shareholder, since his would be an absolute right to be bought out, subject only to the possibility of a renewable two-year waiver. This denial of the corporation's unlimited right to opt out of the mandatory buy-out would seem to be an unwarranted interference with the parties' freedom of contract and a tilting of the scales too far in favor of the minority. See Easterbrook & Fischel, *supra* note 24, at 298. The presence of an unrestricted opt-out privilege would strike a better balance and would still provide meaningful protection for the minority by reversing the existing presumption in favor of the majority. See Olson, *supra* note 198, at 630 n. 19. The result would be that the majority would be required to initiate action to deprive the minority of its statutory buy-out protection, which would promote advance planning in the form of an agreement among the shareholders at the inception of the relationship. Thus, the effect would be similar to (but, obviously, much stronger than) that resulting from the enactment in Ohio of a shareholder oppression relief statute. See *supra* text accompanying note 227.

²⁴⁸ See *supra* notes 200 and 237.

²⁴⁹ See *supra* notes 189 and 202.

²⁵⁰ See Olson, *supra* note 189, at 633; O'Neal, *supra* note 25, at 881, 882. There are a number of reasons why even those minority shareholders having an awareness of the opportunity to contract for protection pursuant to 591 will justifiably fail to do so. See Hetherington & Dooley, *supra* note 81, at 36, 37; Peeples, *supra* note 191, at 490.

and, therefore, available to shareholders of all close corporations within the statutory definition.

In making the crucial decision to define the class of corporations to be covered, both extremes present in existing legislation²⁵¹ should be disapproved. The all-corporations approach should be rejected out of hand because of its inclusion, albeit theoretical only, of publicly traded corporations and the consequent fear, real or imagined, of inviting strike suits. At the other extreme, the arbitrary number of shareholders test would seem to be no more acceptable for this purpose than it was found to be for 591.²⁵² Therefore, aside from consistency, which in itself is an important consideration in regard to legislation *in pari materiae*, the 591 eligibility test of no stock exchange listing or trading market for the corporation's shares would seem to be the most fitting definition.²⁵³

The improper conduct giving rise to relief should be effectively identified, using the language found in the newest statutes²⁵⁴ and endorsed by commentators.²⁵⁵ Thus, the statute should cover action of directors or those in control of the corporation that is illegal, oppressive, fraudulent, or unfairly prejudicial to the complainant, whether in his capacity of shareholder, director, officer or employee.²⁵⁶

The relief that may, in its discretion, be crafted by the court upon a showing of actionable oppression, should be the subject of an extensive list.²⁵⁷ Included on the list should be such hands-on measures available to the judge as ordering or setting aside any action on the part of the corporation or its shareholders, directors or officers; removal or appointment of any individual as a director or officer; requiring payment of dividends; and requiring the corporation or one or more of its shareholders to purchase the shares of the petitioner at their fair value and on prescribed terms. Ordering dissolution of the corporation should be authorized as a last resort.²⁵⁸

To encourage the voluntary observance of high standards of conduct

²⁵¹ See *supra* notes 239-41 and accompanying text.

²⁵² See *supra* notes 87 and 88 and accompanying text.

²⁵³ See Hetherington & Dooley, *supra* note 81, at 52, 53.

²⁵⁴ See *supra* notes 200 & 237 referring to the oppression relief provisions of various state statutes and the MODEL ACT SUPPLEMENT. All are deserving of careful consideration. The newest and most comprehensive of the laws are Minn. Stat. Ann. § 302A.751 (West 1985) and MODEL ACT SUPPLEMENT § 40.

²⁵⁵ See Olson, *supra* note 189, at 632, 633; Mann, *supra* note 18, at 325.

²⁵⁶ This language is substantially the same as that contained in Section 40 of the MODEL ACT SUPPLEMENT, except that in the SUPPLEMENT's final draft the word "employee" was dropped without explanation. The deletion, which has been criticized, would appear to have significantly weakened the protection afforded a minority shareholder. See Kessler, *supra* note 39, at 692, 693. The comparable provisions contained in the Minnesota, New Jersey, and North Dakota laws all contain the reference to "employee."

²⁵⁷ See MODEL ACT SUPPLEMENT §§ 41, 42, 43.

²⁵⁸ *Id.*

among shareholders and to discourage nuisance litigation, there should be a provision permitting the court to award attorney's fees and other expenses to any party. The basis for such an award should be a finding that the losing party has been guilty of aggravated misconduct, either in engaging in the acts complained of or in initiating the suit.²⁵⁹

VIII. CONCLUSION

Rarely would the shareholders of a close corporation in its organizational state not be greatly benefitted by thoughtful planning to tailor the corporate form to their special needs. The good news is that in 591, Ohio has for this purpose the most favorable law of all the states. It is easy to use and highly effective. Unlike the situation prior to 591's adoption, counsel need not be a corporate law expert nor be required to devote an inordinate amount of time in order to produce a document that is totally responsive to the clients' needs.²⁶⁰

The bad news is that, when engaged to form a close corporation, Ohio attorneys may no longer safely be mere scriveners comfortably following an old form. Inaction is, in effect, an election to be governed by the corporate norms provided under the standard provisions of the OGCL and the common law of corporations, inappropriate for the close corporation as they may be. Attorneys, therefore, have an affirmative duty to call to their clients' attention the options made available under 591 and to suggest an agenda for their consideration.²⁶¹ Hopefully, that initiative

²⁵⁹ The exact language should be carefully drafted to assure that the provision acts as a deterrent to misconduct on the part of any of the parties involved. MODEL ACT SUPPLEMENT § 41(b) is typical of the statutory provision that has been enacted for this purpose. It provides that "[i]f the court finds that a party to the proceedings acted arbitrarily, vexatiously, or otherwise not in good faith, it may award one or more other parties their reasonable expenses, including counsel fees and the expenses of appraisers or other experts, incurred in the proceeding." See also MINN. STAT. ANN. § 302A. 751 Subd. 4 (West 1985); N.J. REV. STAT. § 14A:12-7(10)(West 1969 & Supp. 1985); N.D. CENT. CODE § 10-19.1-115(4)(1985). Although this language appears to contemplate an award of expenses to either the defendant or the plaintiff, the phrase used to describe the improper conduct does not seem particularly apt to cover the oppressive action by the defendant that prompted initiation of the suit. Moreover, the legislative comments and notes following the Minnesota and New Jersey sections refer only to the relief given by the section to a defendant who has been harassed by a "strike suit".

²⁶⁰ For comments concerning the ethical and malpractice implications of an attorney's conduct in organizing a close corporation having more than one shareholder, see *supra* note 64.

²⁶¹ See O'Neal, *Preventive Law: Tailoring the Corporate Form of Business to Assure Fair Treatment of All*, 49 MISS. L.J. 529, 529-30 (1979). There is nothing remarkable about this observation. Certainly, if the clients were to choose the partnership form of organization, any responsible attorney would have no choice but to prepare a partnership agreement confronting essentially the same issues. See *supra* note 119 and accompanying text regarding the role of the 591(C) "laundry list" in advising clients.

will culminate in a close corporation agreement, which will provide the foundation for the successful long-term relationship of the parties.²⁶²

In spite of the great advances accomplished by 591, it must be recognized that permissive, preventive law measures are far from a complete answer to the needs of close corporation shareholders. A balanced response to those needs must also include self-executing flexible statutory relief for oppressed shareholders.²⁶³ Here, the OGCL, in sharp contrast to most other states, is shockingly deficient. In fact, it is no exaggeration to state that in this area the OGCL is more in need of repair than were its close corporation planning provisions prior to the enactment of 591.

Both commitment on the part of counsel to the use of the planning opportunities now offered by 591 and creation of an effective statutory remedy to neutralize shareholder oppression are needed to place Ohio in the forefront of states providing enlightened treatment for the close corporation and its shareholders.

²⁶² Professor O'Neal has stressed the need for "resourcefulness and creativity" on the part of the draftsman. O'Neal, *supra* note 261, at 558. For the Ohio attorney, 591 has largely eliminated the need for resourcefulness by providing the close corporation agreement as the perfect device for his or her task. Creative lawyering, however, is still at a premium when it comes to structuring and drafting the substantive aspects of the shareholder relationship.

²⁶³ Commentators have for a number of years stressed the need for close corporation legislation to provide both the opportunity for planning and self-executing protection against unfair treatment of minority shareholders. See Bradley, *A Comparative Assessment of the California Close Corporation Provisions and a Proposal for Protecting Individual Participants*, 9 *Loy. L. Rev.* 865 (1975); Mann, *supra* note 18, at 338.

APPENDIX A

O.R.C. § 1701.591

Close Corporation Agreement

(A) In order to qualify as a close corporation agreement under this section, the agreement shall meet the following requirements:

(1) Every person who is a shareholder of the corporation at the time of the agreement's adoption, whether or not entitled to vote, shall have assented to the agreement in writing;

(2) The agreement shall be set forth in the articles, the regulations, or another written instrument;

(3) The agreement shall include a statement that is to be governed by this section.

(B) A close corporation agreement that is not set forth in the articles or the regulations shall be entered in the record of minutes of the proceedings of the shareholders of the corporation and shall be subject to the provisions of division (C) of section 1701.92 of the Revised Code.

(C) Irrespective of any other provisions of this chapter, but subject to division (D)(2) of this section, a close corporation agreement may contain provisions, which shall be binding on the corporation and all of its shareholders, regulating any aspect of the internal affairs of the corporation or the relations of the shareholders among themselves, including the following:

(1) Regulation of the management of the business and affairs of the corporation;

(2) The right of one or more shareholders to dissolve the corporation at will or on the occurrence of a specified event or contingency;

(3) The obligation to vote the shares of a person as specified, or voting requirements, including the requirement of the affirmative vote or approval of all shareholders or of all directors, which voting requirements need not appear in the articles unless the close corporation agreement is set forth in the articles;

(4) The designation of the persons who shall be the officers or directors of the corporation;

(5) The authority of any individual who holds more than one office of the corporation to execute, acknowledge, or certify in more than one capacity any instrument required to be executed, acknowledged, or certified by the holders of two or more offices;

(6) The terms and conditions of employment of an officer or employee of the corporation without regard to the period of his employment;

(7) The declaration and payment of dividends or distributions or the division of profits;

(8) Elimination of the board of directors, restrictions upon the exercise by directors of their authority, or delegation to one or more shareholders or other persons of all or part of the authority of the directors;

(9) Conferring on any shareholder or his agent the absolute right,

without the necessity of stating any purpose, to examine and copy during usual business hours any of the corporation's records or documents to which reference is made in section 1701.37 of the Revised Code;

(10) Prohibition of or limitation upon the issuance or sale by the corporation of any of its shares, including treasury shares, without the affirmative vote or approval of the holders of all or a proportion of the outstanding shares or unless other specified terms and conditions are met;

(11) Arbitration of issues on which the shareholders are deadlocked in voting power or on which the directors or other parties managing the corporation are deadlocked.

(D) Except as may be necessary to give effect to divisions (C)(3), (5), (8), and (9) and division (I) of this section, any provision of a close corporation agreement that does either of the following shall be invalid:

(1) Eliminates the filing with the secretary of state of any document required under this chapter or changes the required form or content of the document;

(2) Waives or alters the effect of any of the provisions of section 1701.03, 1701.18, 1701.24, 1701.25, 1701.30, 1701.31, 1701.32, 1701.33, 1701.35, 1701.37, 1701.38, 1701.39, 1701.591 [1701.59.1], 1701.91, 1701.93, 1701.94, 1701.95, or the first sentence of section 1701.64 of the Revised Code.

Unless otherwise provided in the close corporation agreement, the invalidity of a provision pursuant to this division does not affect the validity of the remainder of the agreement.

(E) Unless a close corporation agreement requires the affirmative vote or written consent of the holders of a greater proportion of the shares of any class, it may be amended or terminated by the affirmative vote or written consent of the holders, then parties to the close corporation agreement, of four-fifths of the outstanding shares of each class. If a close corporation agreement is amended or terminated by the written consent of the holders of fewer than all shares, the secretary of the corporation shall mail a copy of the amendment or a notice of the termination to each shareholder who did not so consent. If a close corporation agreement set forth in the articles is amended, the amendment shall not be effective unless it is filed as an amendment to the articles pursuant to section 1701.73 of the Revised Code.

(F) No close corporation agreement is invalid among the parties or in respect of the corporation on any of the following grounds:

(1) The agreement is an attempt to treat the corporation as if it were a partnership or to arrange the relationship of the parties in a manner that would be appropriate only among partners;

(2) The agreement provides for the conduct of the affairs of a corporation or relations among shareholders in any manner that would be inappropriate or unlawful under provisions of this chapter other than

those set forth in division (D)(2) of this section or under other applicable law;

(3) The agreement interferes with the authority or discretion of the directors;

(4) The agreement has not been filed with the minutes as required by division (B) of this section.

(G) If a close corporation agreement provides that there shall be no board of directors, both of the following apply to the shareholders:

(1) They are, for the purposes of any statute or rule of law relating to corporations, deemed to be the directors to the extent not inconsistent with the close corporation agreement;

(2) They have all of the liabilities of directors.

(H) The existence of a close corporation agreement shall be noted conspicuously on the face or the back of every certificate for shares of the corporation and a purchaser or transferee of shares represented by a certificate on which such a notation so appears shall be conclusively considered to have taken delivery with notice of the close corporation agreement. Any transferee of shares by gift, bequest, or inheritance and any purchaser or transferee of shares with knowledge or notice of a close corporation agreement is bound by the agreement and shall be considered to be a party to the agreement.

(I) A close corporation agreement becomes invalid if shares of the corporation are listed on a national securities exchange, are regularly quoted in an over-the-counter market by one or more members of a national or affiliated securities association, or are transferred or issued to a person who takes delivery of the certificate for the shares other than by gift, bequest, or inheritance and without knowledge or notice of the close corporation agreement and that person does not consent in writing to the close corporation agreement within thirty days after the date on which a certificate for the shares has been issued in the name of that person or his nominee.

In the event of such invalidity and unless otherwise provided in the close corporation agreement, any provision contained in the agreement that would not be invalid under any other section of this chapter or under other applicable law remains valid and binding on the parties to the close corporation agreement.

Any officer of the corporation who learns of the occurrence of any event causing the invalidity of the close corporation agreement shall immediately give written notice of such invalidity to all of the shareholders.

If a close corporation agreement set forth in the article of the corporation becomes invalid, the officers of the corporation shall promptly sign and file the certificate of amendment prescribed by section 1701.73 of the Revised Code, setting forth the reason for invalidity and deleting the close corporation agreement from the articles. If the officers fail to execute and file the certificate within thirty days after the occurrence of the event giving rise to the invalidity, the certificate may be signed and

filed by any shareholder and shall set forth a statement that the person signing the certificate is a shareholder and is filing the certificate because of the failure of the officers to do so.

(J) A close corporation agreement, in the sound discretion of a court exercising its equity powers, is enforceable by injunction, specific performance, or other relief that the court may determine to be fair and appropriate.

(K) The failure of a corporation, pursuant to a close corporation agreement, to observe corporate formalities relating to meetings of directors or shareholders in connection with the management of the corporation's affairs shall not be considered a factor tending to establish that the shareholders have personal liability for corporate obligations.

(L) This section shall not be construed as prohibiting any other lawful agreement among two or more shareholders.

(M) No corporation with respect to which a close corporation agreement is in effect, shall issue shares in uncertificated form, and any resolution of the directors of such a corporation, providing for the issuance of shares in uncertificated form, shall be ineffective during such period as a close corporation agreement is in effect. The adoption of a close corporation agreement shall act as a transfer instruction to such corporation to replace uncertificated securities with appropriate certificated securities in accordance with division (C) of section 1308.43 of the Revised Code.

(N) The amendments to this section that are effective April 1, 1985 are remedial in nature and apply to all close corporations created on or after November 17, 1981.

APPENDIX B

FORM OF SINGLE SHAREHOLDER CLOSE
CORPORATION AGREEMENT*Articles of Incorporation*²⁶⁴
of
Gun, Inc.

(a corporation governed by a close corporation agreement pursuant to § 1701.591, R.C.)

The undersigned, desiring to form a corporation for profit under the General Corporation Law of Ohio and to adopt a close corporation agreement pursuant to § 1701.591 of the Revised Code, does hereby certify and agree as follows:

Article One
Name

The name of said corporation shall be GUN, Inc.

Article Two
Principal Office

The place in the state of Ohio where its principal office is to be located is the city of Cleveland, Cuyahoga County.

²⁶⁴ The person adopting the agreement is required by 591(A) to be a shareholder at the time of adoption. However, under O.R.C. § 1701.09, it is not until after the articles have been filed that subscriptions for shares can be received. Therefore, it is necessary that, following the acceptance of the subscription and issuance of the shares, the sole shareholder, in writing, confirm and adopt the close corporation agreement. This procedure will avoid the necessity, following the issuance of shares, to file amended articles of incorporation embodying the close corporation agreement. Corporations Counsel to the Office of the Ohio Secretary of State has expressed his satisfaction with this procedure, and also with the acceptability for filing of the form of articles of incorporation in Appendix B. He has also recommended that all documents filed for the corporation with the Secretary of State subsequent to the filing of the original articles refer in their preamble to the recording data applicable to the original filing. Such a reference would eliminate the need for an accompanying affidavit to justify the signing of the filed document by only one person. See *supra* note 124.

Article Three
Purpose

The purpose for which it is formed is to engage in any lawful act or activity for which corporations may be formed under §§ 1701.01-1701.98 of the Revised Code.

Article Four
Number of Shares

The maximum number of shares which the corporation is authorized to have outstanding is 750 shares, all of which shall be common shares without par value.

Article Five
Close Corporation Agreement

The undersigned, Annie Gun, being the intended sole shareholder of the corporation, does hereby adopt and assent to the following close corporation agreement:

1. This agreement shall be governed by § 1701.591 of the Revised Code of Ohio.
2. The corporation shall have no board of directors.
3. The corporation shall have no code of regulations.
4. Annie Gun shall be the president, secretary and treasurer of the corporation, and there shall be no other officer of the corporation.
5. Annie Gun shall have the authority to execute, acknowledge, or certify in all of her respective capacities as said three officers any instrument required for any purpose to be executed, acknowledged, or certified by the holders of two or more offices of the corporation.
6. The execution of any instrument by Annie Gun on behalf of the corporation shall be the only act required to make such instrument binding on the corporation and all persons dealing with the corporation may rely thereon without further inquiry.
7. This agreement shall be effective upon the issuance of shares of the corporation to Annie Gun.

IN WITNESS WHEREOF, I have hereunto subscribed my name this first day of October, 1986.

Annie Gun

APPENDIX C

FORM OF MULTI-SHAREHOLDER CLOSE
CORPORATION AGREEMENT²⁶⁵

Hypothetical underlying facts: Abel is 40 years old and contributing to the venture his present manufacturing business, previously operated as a sole proprietorship and having a present book value of \$150,000; Baker is 50 years old, is contributing \$200,000 in cash, intended primarily as a passive investment, although he will provide financial and managerial guidance; Charley, 45 years old, is an experienced sales executive, who is making a cash investment of \$10,000 and, in addition, has resigned his present position to serve as sales manager of the corporation. The parties have selected the corporate form to achieve limited liability and perceived tax benefits.

CLOSE CORPORATION AGREEMENT
(pursuant to § 1701.591, R.C.)

THIS AGREEMENT is entered into at Cleveland, Ohio on the 1st day of October, 1986, by and among, ABC, Inc., an Ohio corporation, and Abel, Baker and Charley, all of Cleveland, Ohio.

RECITALS

1. Abel, Baker and Charley (collectively the "Shareholders" and sometimes individually "Shareholder") are all of the Shareholders of ABC, Inc. (the "Corporation"), a newly formed Ohio corporation, which they desire to be the subject of a close corporation agreement pursuant to § 1701.591, R.C.

2. The total number of issued and outstanding shares of capital stock of the Corporation ("shares") is 100, of which Abel owns 45, Baker owns 45 and Charley owns 10.

²⁶⁵ This form is intended to illustrate how the unique features of 591 can be implemented. The reader is cautioned that some of the form's key provisions (*e.g.*, employment and compensation) are lacking in detail. Other forms of a multi-shareholder close corporation agreement under 591 appear in Z. & M. CAVITCH, OHIO CORPORATION LAW WITH FEDERAL TAX ANALYSIS (1986) (Form No. 13a) and J. BLACKFORD, *Ohio Corporation Law and Practice* (1985)(Form F 42.01).

OPERATIVE PROVISIONS

1. *Close Corporation Agreement.* This Agreement is a close corporation agreement governed by § 1701.591 of the Revised Code of Ohio.

2. *No Code of Regulations.* The Corporation shall have no code of regulations.

3. *No Board of Directors.* The Corporation shall have no board of directors.

4. *Officers and Employment.* The officers of the Corporation shall be: Abel - President, Treasurer and Assistant Secretary; Baker - Executive Vice President and Secretary; and Charley - Vice President, Sales. None of the Shareholders shall take any action on behalf of the Corporation in his capacity as an officer, which shall be inconsistent with the provisions of this Agreement. Abel and Charley shall work full-time, and Baker shall work part-time, for the Corporation.

5. *Compensation.* The annual salaries payable to the Shareholders by the Corporation shall be: Abel - \$80,000; Baker - \$20,000; and Charley - \$70,000; and the same may be changed only by action taken pursuant to Section 7 below. Charley shall receive, in addition to his annual salary, a bonus equal to 2% of annual sales in excess of \$5,000,000, provided that such bonus in no event shall exceed an amount equal to one-half the salary payable to Charley for the corresponding fiscal year.

6. *Distributions.* Following the end of each fiscal year of the Corporation, there shall be distributed to the shareholders, so long as the net worth of the Corporation at year end shall be at least \$400,000, an amount equal to one-fourth of the Corporation's net profit for the previous year, and, if said net worth shall at year end be at least \$600,000, an amount equal to one-half of such net profit. Such distribution shall be payable 45% to Abel, 50% to Baker and 5% to Charley.²⁶⁶

7. *Authorizing Action.* Except as otherwise provided in this agreement, all action on behalf of or with respect to the Corporation that would under Ohio law ordinarily require action by a board of directors or shareholders shall be taken only with approval of both Abel and Baker; except that the unanimous approval of all the Shareholders shall be required for (a) the issuance of any stock (including treasury shares) of the Corporation, (b) the redemption of any Shareholder's shares, (c) an amendment to the Article of Incorporation, (d) the dissolution of the Corporation, (e) a sale of all or substantially all of the assets of the Corporation, (f) a merger or consolidation of the Corporation, or (g) an increase, directly or indirectly, in the compensation payable to any of the shareholders that shall not be proportionate to the salaries established in section 5 above.

²⁶⁶ As a "division of profits" otherwise than in accordance with shareholdings, this provision is clearly authorized under 591(C)(7). However, it would likely make the corporation ineligible for Internal Revenue Code Subchapter S status. See *supra* note 111.

8. *Action in Writing and Notification.* Action taken by the Shareholders hereunder shall be evidenced by the written consent of those Shareholders whose approval is necessary, and where the concurrence of only Abel and Baker is necessary, prompt notification in writing of such action shall be given to Charley.

9. *Transfers of Shares.* No Shareholder shall, voluntarily or involuntarily, transfer his shares except in accordance with the following provisions:

(Appropriate provisions should include, among other things, restrictions on the transfer of shares; and purchase rights and obligations in the event of death, permanent disability or termination of employment of any of the Shareholders, and possibly, upon the happening of other events.)

10. *Examination of Records.* Any Shareholder or his agent shall have the absolute right during usual business hours without the necessity of stating any purposes, to examine and copy any of the Corporation's records or documents.

11. *Execution in Multiple Capacities.* Each of Abel and Baker, who, as above provided, hold two offices of the Corporation, is hereby authorized to execute, acknowledge or certify in both of his capacities, any instrument required for any purpose to be executed, acknowledged, or certified by the holders of two or more offices of the Corporation.

12. *Termination.* Unless the Corporation is dissolved or this Agreement is terminated earlier pursuant to the provisions hereof, this Agreement shall continue in existence until September 30, 2000. At that time, unless Abel and Baker otherwise agree, the Corporation shall be dissolved. If the Corporation shall not be dissolved and Charley does not wish to continue as a shareholder, he shall sell and the Corporation shall purchase his shares for cash at a price equal to the fair value thereof, which, if the Shareholders cannot agree, shall be determined by arbitration as provided in Section 13 below. Abel and Baker shall jointly and severally be liable to purchase any of Charley's shares that the Corporation cannot legally purchase, and, as between themselves, Abel and Baker shall each acquire one-half of such shares or as they may otherwise agree.

13. *Arbitration.* In the event of a deadlock in voting power among the Shareholders, the issue, at the option of either Abel or Baker, shall be decided by binding arbitration in accordance with the rules of the American Arbitration Association. Any other dispute arising under this Agreement shall likewise be decided by arbitration initiated by any Shareholder. If the arbitrator(s) shall find that any party to the proceeding has acted arbitrarily, vexatiously or otherwise not in good faith, either in initiating or pursuing the arbitration or in taking the position or action resulting in the deadlock or dispute that is the subject of the arbitration, the arbitrator(s) may assess against such party all or part of

the reasonable expenses, including counsel and witness fees, incurred in the proceeding by one or both other parties. Otherwise, such expenses shall be paid by the corporation.

14. *Legend and Notification.* The following legend shall be conspicuously noted on all stock certificates evidencing shares of the Corporation:

"The shares of stock represented by this certificate are subject to, and are transferable (if at all) only in compliance with, a Close Corporation Agreement, dated as of October 1, 1986, among the Corporation and all of its shareholders, a copy of which has been entered in the record of minutes of the proceedings of the shareholders of the corporation. Any attempted transfer in violation of the provisions of said Agreement shall be null and void and of no effect and, in any event, any transferee or purported transferee of the shares evidenced hereby shall be bound by said Agreement. The Corporation will mail to any shareholder a copy of the Agreement without charge within five days of the receipt of written request therefor."

With knowledge that the transfer of shares evidenced by a certificate that does not carry a legend noting the existence of this Agreement could result in the invalidation of the Agreement, each Shareholder agrees that if he transfers shares represented by a certificate, which for any reason does not bear such a legend, he will notify in writing such transferee of the existence of this Agreement and deliver a copy thereof to him at the time of such transfer. Any Shareholder's failure to do so will render him liable to the Corporation and to the remaining Shareholders for compensatory and punitive damage.

15. *Further Assurances.* The parties shall execute and deliver such other instruments and take such other action as may be necessary or convenient to effectuate all the provisions of this Agreement.

16. *Indemnification.* Abel and Baker, jointly and severally, agree to indemnify Charley against any liabilities of directors arising under division (G)(2) of § 1701.159 R.C. as a result of action taken by Abel and Baker in which, pursuant to Section 7 of this Agreement, Charley had no right to and did not participate.

17. *Equitable Relief.* The parties acknowledge that it is impossible to measure in money the damages that would result by reason of a party's breach. It is therefore agreed that the provisions of this Agreement shall be enforceable by injunction, specific performance or other equitable relief, without reference to whether or not an adequate remedy at law may be available. It is further agreed that any such equitable relief may be awarded in the arbitration proceedings authorized hereunder.

18. *Governing Law.* This Agreement shall be governed by and construed in accordance with the laws of the State of Ohio.

19. *Amendment or Termination.* This Agreement may be amended or

terminated only by the unanimous agreement of the Shareholders, which must be evidenced by a writing signed by all of them.

20. *Heirs and Successors.* This Agreement shall inure to the benefit of and be binding upon the respective heirs, personal representatives, successors and assigns of the parties hereto.

21. *Entire Agreement.* This Agreement is the entire and exclusive statement of the parties' agreement and it supersedes all prior agreements, understandings, negotiations and discussions among the parties, whether oral or written.

22. *Section Headings.* The section headings in this Agreement are provided for convenience only and shall be disregarded in the interpretation of the Agreement.

IN WITNESS WHEREOF, the parties hereto, intending to be legally bound, have executed this Agreement as of the date at the beginning thereof.

ABC, Inc.

by _____
President

Abel

Baker

Charley